KING COUNTY,
WASHINGTON

RISK MANAGEMENT AUDIT

September, 1999

October 15, 1999 736-001

Metropolitan King County Council Members
King County Courthouse
Seattle, Washington 98104

RISK MANAGEMENT AUDIT

Dear Council Members:

On behalf of the ARM Tech audit team, we are pleased to submit the Risk Management Audit report.

The purpose of the study was to evaluate the County's overall structure and approach to managing risks of property, liability and workers compensation loss. The analysis included the following subjects:

- Program costs.
- Staffing, other resources and practices used to manage risk.
- Loss prevention practices and staffing.
- Claims management practices and staffing.
- Self-insurance and insurance program design.

Activities leading to this report have included:

- Interviews with key personnel in the Risk Management Division, Safety & Claims Division, Prosecuting Attorney's Office and most of the department directors and division managers in King County.
- Review of insurance policies, program summaries and other pertinent data supplied by the County.
- Review and analysis of the County's September 1998 actuarial report and other loss and exposure data.
- Case review of liability and workers compensation claims.
- Visits to a cross-section of County facilities.
- Review of the County's risk data systems, administrative practices, staffing budgets and other pertinent information.

At $30 million or 1.9% of operating expenditures, the County's 1998-1999 cost of liability, property and workers compensation risk is better than average versus similar entities. Recent liability claims have the potential to deplete the County's primary and catastrophic liability funds. The County's actuary projects outstanding workers compensation losses at $9 million greater than the County has reflected in its financials. With these developments, the County will have to consider higher levels of funding for its programs.

Overall, the County is devoting appropriate level of staff and other resources to manage risks. However, we have recommended some important changes be considered in the areas of parity among departments that manage risk, reporting relationships and several current risk management practices.

The executive response is appended to our report.

Work on this project was directed by Michael Kaddatz. Steven Glicksman analyzed the actuarial review and adequacy of and approach to funding. Timothy Farley evaluated the administration and management of claims. Peter Junker led the field work and analysis on the risk management organization, loss prevention, insurance protection and program costs.

We appreciate the opportunity to assist the County and thank the County Auditor's Office, Risk Management, Safety & Claims, Prosecuting Attorney's Office and other King County personnel involved in this project for their participation and support.

Respectfully submitted,

ADVANCED RISK MANAGEMENT TECHNIQUES, INC.

By ______________________________

Michael M. Kaddatz, CPCU, ARM
Principal

By ______________________________

Peter F. Junker, ARM
Senior Consultant

By ______________________________

Timothy P. Farley, CPCU
Senior Claims Consultant

MMK/PFJ/TPF:arm
C:\0DataDir\King.wpd

TABLE OF CONTENTS

Exhibits

Appendix

I. EXECUTIVE SUMMARY

In this section of the report, we highlight the purpose of the audit and major findings of each chapter. A summary of findings and recommendations is listed in Chapter II.

The purpose of this study is to evaluate the County's overall structure and approach to managing risks of property, liability and workers compensation loss. The analysis included the following subjects:

- Program costs.
- Risk management organization.
- Loss control.
- Claims management.
- Risk financing.

Program Costs

The property, liability and workers compensation programs comprise current annual County expense of $30.0 million, or 1.9% of the operating budget (total appropriation for all program plan areas). This cost, usually referred to as the "cost of risk", includes insurance premiums, self-insured losses and all directly related administrative expenses.

By comparison, for public entities the size of the County, the cost of risk usually ranges from 1.5% - 3.5% of the operating budget.

- The level of risk costs at the County indicate it is effectively managing risk (see page 10).

Risk Management Organization

The County has a manager for the property and liability program (Risk Manager) and another for the workers compensation program (Manager of Safety & Claims). This is an appropriate division of responsibility.

Although they have separate areas of responsibility, Risk Management and Safety & Claims have common concerns primarily in the area of loss control. Operations at the County facilities create situations that simultaneously expose employees and the public to loss.

- The managers of Risk Management and Safety & Claims should establish a formal plan to meet regularly to discuss common exposures and loss control measures (see page 25).

The Safety & Claims Manager is a non-voting member of the Risk Management Committee. However, the workers compensation costs are about $12 million, or around 40% of the County's total risk costs. The common challenges of liability and workers compensation and the synergy that can result by developing joint solutions has great potential for the County. All on the committee should be empowered to seek global solutions.

- The Safety & Claims Manager should be included as a voting member of the Risk Management Committee (see page 26).

Risk Management is a division of the Information and Administrative Services Department. However, Risk Management manages all risks of property and liability loss emanating from all departments. Risk Management is also charged with managing County resources to buy insurance, to pay liability losses and to protect the public and the County's property via loss prevention activities. Risk Management would have better visibility and perceived as having stronger authority to accomplish its objectives if it was moved from a line department to an area that is recognized for providing broad general services.

- Risk Management should be made part of the County Executive office. (see page 26).

Loss Control

Risk Management is charged with the responsibility for the "reduction of risk and exposure to loss, including programs and precautions for safety to reduce hazards to the public that may exist in county facilities and operations." A loss control contingency fund of $100,000 assists Risk Management in its leadership role by providing a source to finance acute loss control needs. Additional funding would allow Risk Management to have an even greater impact in this area.

Although Safety & Claims shares the same responsibility for controlling losses as Risk Management, it does not have a similar fund.

- The loss control contingency fund should be increased to $300,000; used for both liability and workers' compensation needs and jointly funded by the two programs (see page 41).

Claims Management

A claims procedures manual does not exist for either Risk Management or Safety & Claims. Such a document would help shield the County from any accusations of bad faith claims handling. A manual would also be valuable as a reference to instruct new employees on claims handling policies of the County.

- We strongly recommend the adoption of claims procedures manuals for both Risk Management and Safety & Claims (see pages 58 and 80).

Accepted claims handling standards require contact of all claimants within 24 hours of the receipt of loss notice. This standard is not being met on a consistent basis by either Risk Management or Safety & Claims.

- We recommend that the County adopt the standard of contacting claimants within 24 hours after notice of loss is received and include it as a written procedure in the claims procedure manual (see page 77).

The County handles its own liability (other than Metro) and workers compensation claims and is effective at managing them. Since the merger with the County, Metro liability claims continue to be handled by an outside administrator. We have determined that, if the County brought these claims in-house, almost $200,000 would be saved annually (not including one-time equipment costs).

- The County should bring the Metro liability claims handling function in-house (see page 69).

Risk Financing

One of the main reasons for this audit was the County's concern regarding the adequacy of its loss reserves and a review of other risk funding options. The County's funding is divided into three areas: primary liability (claims up to $1 million), catastrophe liability (claims in excess of $1 million) and workers compensation.

Generally speaking, the County's funding for liability losses has been adequate and not excessive. Their approach is considered conservative since some large public entities opt not to set aside money to pay for future losses (a discussion of funding options is included in Chapter VII). Below is our review of the current status of the liability loss funds:

- The recent deterioration in County liability loss experience threatens the small ($600,000) equity balance in the primary liability fund (see page 86).

- Incidents with potentially catastrophic results could well exceed the current $2 million surplus in the catastrophe fund (see page 86).

The County's approach to funding for workers' compensation losses is used by some entities but is inconsistent with the method used for liability losses. Their approach in this area is aggressive and not excessive at all. Below is our review of the current status of the workers' compensation loss fund:

- The County's actuary projects workers compensation outstanding losses to be $9 million greater than the amount that is reflected in the County's financial statements. After allowing for investment income, the difference is reduced to about $7 million (see page 87).

Chapter VII has a discussion of the advantages and disadvantages of various funding options available to the County.

The recommendations in this Chapter and Chapter II are detailed in the body of the report. The report should be read in its entirety to obtain a complete understanding of our findings.

II. SUMMARY OF FINDINGS AND RECOMMENDATIONS

This section highlights all of the recommendations that are included in the Executive Summary (*in italics)* as well as those that are included in the body of the report.

Chapter Findings & Recommendations		Page #
Program Costs — Chapter III		
1.	*The level of risk costs at the County indicate it is effectively managing risk.*	10
2.	The loss rates for 1998 and 1999 for property, liability and workers compensation combined are the lowest they have been in the last nine years.	20
Risk Management Organization — Chapter IV		
3.	*The managers of Risk Management and Safety & Claims should establish a formal plan to meet regularly to discuss common exposures and loss control measures.*	25
4.	*The Safety & Claims Manager should be included as a voting member of the Risk Management Committee.*	26
5.	*Risk Management should be made part of the County Executive office.*	26
6.	Involve the Safety & Claims Manager in the analysis and decision-making process when purchasing excess workers compensation insurance.	29
7.	Risk Management should prepare an annual report for the County Executive and department managers that would include cost of risk, claims frequency and loss control information.	33
8.	Use the most recent five years of loss experience to calculate each department's liability loss allocations.	33
9.	Prepare and distribute suggested Risk Management insurance fund charges by September 1 of each year.	34
10.	Apply a workers compensation loss experience factor when calculating each department's loss rate.	34

Chapter Findings & Recommendations		Page #
11.	Convert to the new risk management information system as soon as possible.	34
12.	Do not limit the contractor's liability insurance requirement to the extent of the contractor's negligence.	37
13.	Perform periodic audits to ensure that contract insurance requirements are being met.	37
14.	Discontinue the practice of monitoring insurance from subcontractors.	37
15.	The County is receiving the quality and quantity of service necessary from its broker at a very reasonable cost.	38
Loss Control — Chapter V		
16.	The County has sufficient loss control personnel in place in Risk Management, Safety & Claims safety officers.	40, 42
17.	*The loss control contingency fund should be increased to $300,000 and used for both liability and workers compensation needs.*	41
18.	Hold meeting on a regular basis between former Metro division safety personnel and Safety & Claims safety officers.	42
19.	Evaluate supervisor training on employment practices to ensure compliance by all departments.	43
20.	Use an outside service for reporting of discrimination concerns by employees. Establish an in-house position responsible for investigating such situations.	43
Claims Administration and Management — Chapter VI		
21.	Monitor workers compensation caseloads to ensure that all officers are maintaining indemnity caseloads below 175.	45
22.	All workers compensation claims personnel are qualified to handle Washington workers compensation claims.	47
23.	Develop an initial workers compensation claim checklist to be completed by the claims supervisor prior to distributing the assignment to the officer.	47

Chapter Findings & Recommendations		Page #
24.	*Adopt the 24-hour standard regarding employee contact after a workers compensation claim has been received and include as a written procedure in the claims procedure manual.*	49
25.	Aggressively pursue subrogation opportunities.	51
26.	*Develop a workers compensation claims handling procedural manual.*	58
27.	*The County should bring the Metro liability claims handling function in-house.*	69
28.	*Adopt the 24-hour standard regarding claimant contact after a liability claim has been received and include as a written procedure in the claims procedure manual.*	77
29.	Initiate procedures whereby all liability claim file material is secured to the file jacket and in chronological order.	80
30.	*Create a liability claims procedure manual.*	80
Risk Financing — Chapter VII		
31.	Fees paid for liability and workers compensation actuarial services are reasonable.	81
32.	Direct the actuary to calculate the net present value of outstanding reserves.	83
33.	Direct the actuary to use the "frequency times severity" and the "Bornhuetter-Ferguson" method to project losses.	84
34.	Outstanding losses as projected by the actuary are within a range of reasonable outcomes.	84
35.	Concise summary tables and improved documentation are needed in the actuarial report.	84
36.	*The recent deterioration in County liability loss experience threatens the small ($600,000) equity balance in the primary liability fund.*	86
37.	*Incidents with potentially catastrophic results could well exceed the current $2 million surplus in the catastrophe fund.*	86

Chapter Findings & Recommendations		Page #
38.	Unallocated loss adjustment expenses (ULAE) need to be included in both the actuarial report and the County's financial statements (per GASB Statement No. 10).	87
39.	*The County's actuary projects workers compensation outstanding losses to be $9 million greater than the amount that is reflected in the County's financial statements. After allowing for investment income, the difference is reduced to about $7 million.*	87
40.	The County should use the actuarial estimate for projected workers compensation losses, discounted for investment income, rather than the in-house staff estimate that does not use actuarial procedures.	88
41.	The County obtain an updated actuarial estimate of funds needed for catastrophe losses and accrue the money necessary to meet future obligations.	91
42.	Streamline the liability insurance document by amending the insuring agreement to cover all liability for damages caused by an occurrence.	94
43.	The County purchases a reasonable amount of liability, workers compensation and property insurance protection.	97, 99, 100
44.	The County purchases a reasonable amount of airport and aviation liability protection.	97
45.	Review annually the availability and pricing of pollution coverage.	98
46.	The County's purchase of excess workers compensation coverage is worthwhile based on a comparison of the premium to recent loss experience.	99
47.	Evaluate potential participation in NAPEX and CRIL, two county "pools" that offer an alternative to standard insurance.	101

III. PROGRAM COSTS

Managing risk is an ongoing process. Monitoring the cost of risk, ultimate losses and loss rates will provide the County with the necessary feedback regarding how successful its risk management program is and where changes might need to be made.

A. COST OF RISK

Cost of risk is a concept that attempts to quantify and tabulate the amounts expended on risk treatment methods. The major risk cost elements are:

1. **Insurance premiums.** Amounts paid to commercial insurers or risk retention pools.

2. **Self-insured losses.** Losses paid under deductibles, self-insured retentions, or from incidents simply not covered by insurance. This loss category also commonly includes legal defense costs and certain other miscellaneous expenses called "allocated loss adjustment expenses" (ALAE).

3. **Administration.** Administrative expenses include contract or in-house staff expenses and related overhead associated with claims adjusting, loss prevention and financial management of risks.

4. **Indirect risk costs.** These are secondary expenses that arise as a result of losses incurred. Examples of indirect costs are:

   - A supervisor's time spent filling out accident reports.

   - Overtime wages or additional employee costs necessary to replace the productivity of an employee lost to an injury.

In this report, we concentrate only on the direct cost of risk (the first three items above). Indirect costs are virtually impossible to tabulate. Note, however, that experts have estimated indirect risk costs at anywhere from two to ten times the direct cost of losses incurred. Since indirect risk costs are a function of losses, measures taken to reduce losses in the first place are the best way of reducing all risk costs, direct and indirect.

Table III-1 tabulates the estimated direct cost of risk for the County. The County's 1998 direct cost of risk is about $30.0 million. This is 1.9% of the County's operating budget ($1.6 billion). For comparison, a large urban California county that was well managed had a cost of risk of 2.2% during the 1996/97 fiscal year.

- The level of risk costs at the County indicate it is effectively managing risk.

Now that the County knows what its cost of risk is, a benchmark has been established. If this factor starts to climb above 2.0%, the County would know that some measures need to be taken to reduce it to its former level. This might include lowering or raising the retention levels, increasing loss control efforts or other measures.

Table III-1
KING COUNTY
1998 Cost of Risk

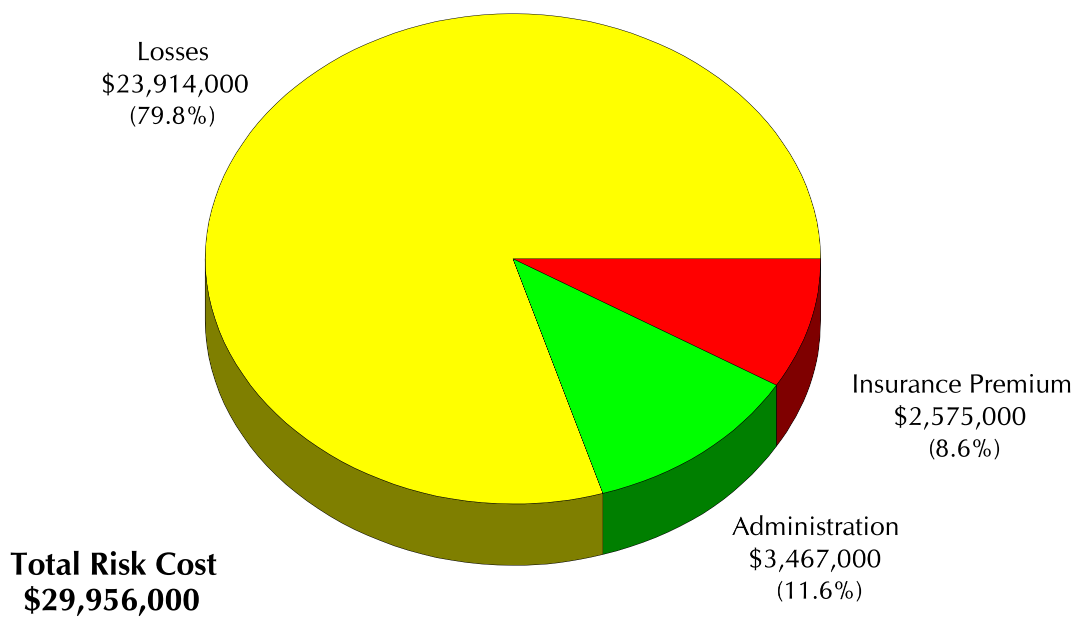
Insurance Premiums[1]	
• Liability	$1,081,000
• Workers Compensation	75,000
• Property	1,419,000
Subtotal	$2,575,000
Self-Insured Losses, Including Allocated Loss Adjustment Expenses	
• Liability[2,3]	$13,944,000
• Workers Compensation[2,4]	9,930,000
• Property[5]	40,000
Subtotal	$23,914,000
Administration	
• Risk Management[5]	$1,085,000
• Workers Compensation[6]	1,682,000
• Service Providers[7]	700,000
Subtotal	$3,467,000
Cost of Risk	$29,956,000
Operating Budget[8]	$1,572,789,000
Cost of Risk Compared to Operating Budget	1.9%

Notes:
1 Obtained from the "Insurance Fund - 1998 Annual Report."
2 Projected losses obtained from Fallquist actuarial study dated 9/3/98 plus ULAE.
3 Obtained from Risk Manager and includes $2,144,000 in Prosecuting Attorney Office defense staff cost.
4 Obtained from Safety & Claims Division and includes $130,000 in Prosecuting Attorney Office defense staff cost.
5 Obtained from Risk Manager.
6 Obtained from Safety & Claims Manager.
7 Obtained from Risk Manager and includes $520,000 in third-party claims administration fees, $137,000 in broker service fees and $43,000 in consulting fees (Risk Management and Safety & Claims combined).
8 Obtained from page B-3 of the "1999 Adopted Budget."

Table III-2 below illustrates the breakdown of the County's cost of risk by expense type. The primary goal of a risk management program is to reduce an organization's cost of risk by achieving optimum balance between premiums, self-insured losses and administration costs.

By far, the largest portion and main factor in driving the County's risk costs are self-insured losses that account for about 80% of the cost of risk. This element can vary widely and reinforces the need for a strong loss control program. Effective loss prevention will reduce the loss portion and could conceivably lead to a reduction in amount of insurance purchased. Both actions will serve to lower the County's cost of risk.

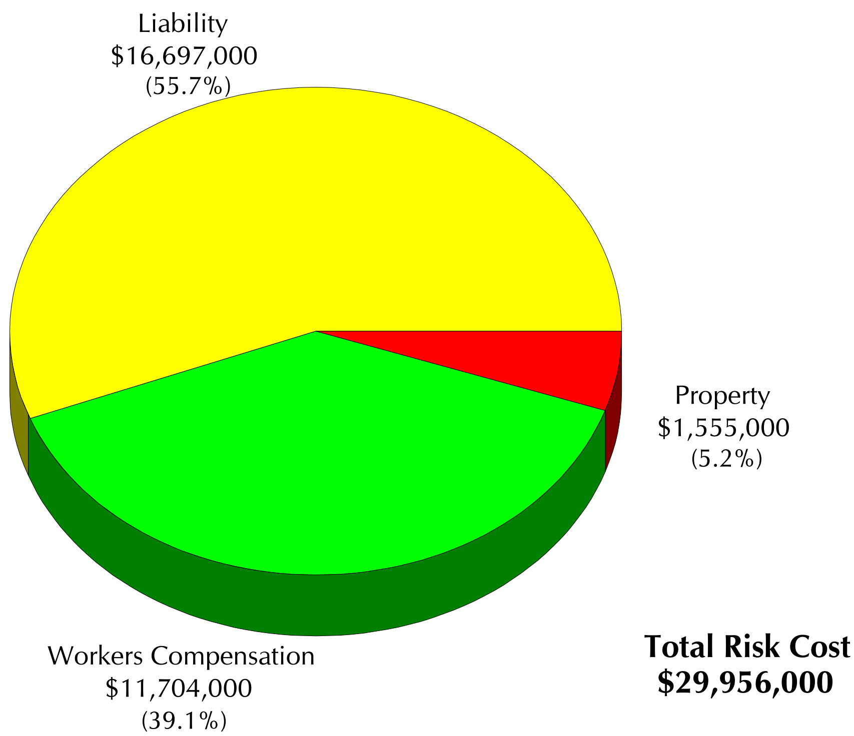
Table III-2
KING COUNTY
1998 Cost of Risk by Expense Type



Tables III-3 below provides a breakdown of the cost of risk between the three major coverage areas. Liability accounts for a little more than half of the cost, workers compensation around 40% and only about 5% of the total cost is attributed to the property program.

This exhibit illustrates that a significant portion of the County's cost of risk is affected by workers compensation. This fact plays into a recommendation detailed in Chapter IV that Safety & Claims should have a greater role in the County's risk management decision-making processes.

Table III-3
KING COUNTY
1998 Cost of Risk by Program

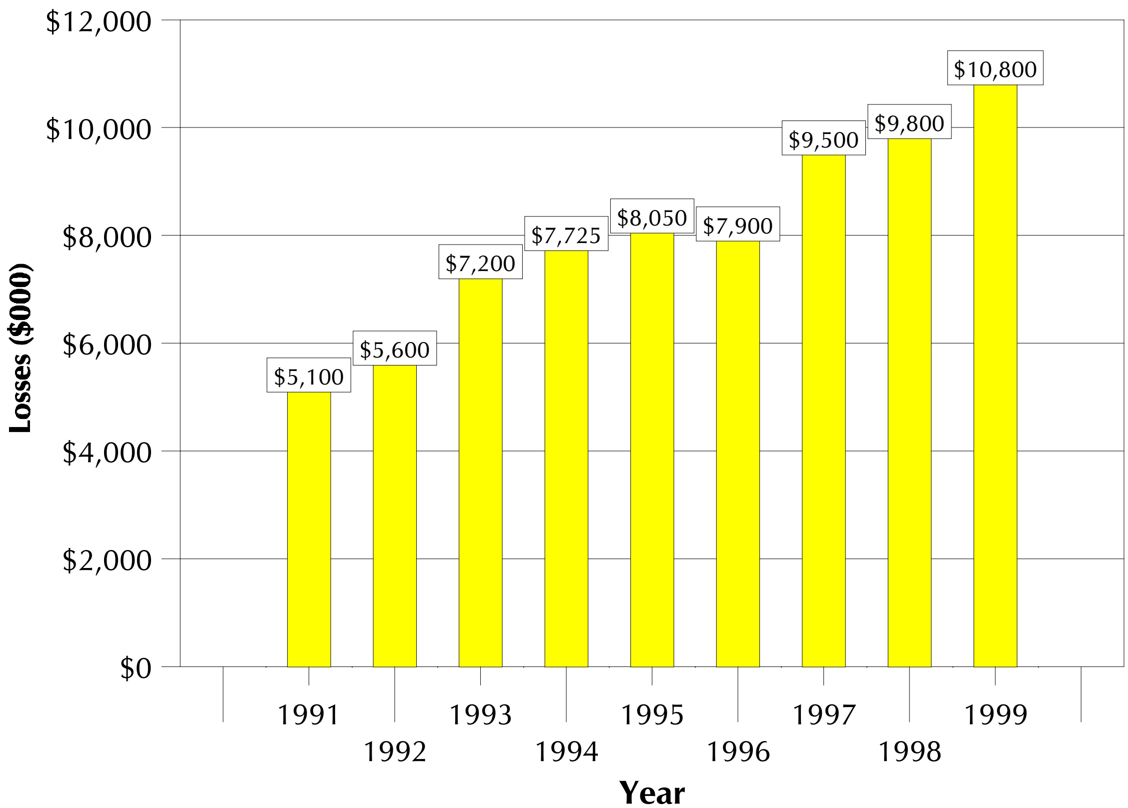


B. PROJECTED ULTIMATE LOSSES

Since self-insured losses represent the largest portion of the County's cost of risk, it is important to know the ultimate losses for each line of coverage. Tables III-4, III-5, III-6 and III-7 include data obtained from the Fallquist actuarial study dated 9/3/98 and provide projections for workers compensation, general liability, automobile liability and all three lines combined. Unallocated loss adjustment expenses (see Chapter VII) are not included in this data.

Table III-4 illustrates that workers compensation losses have increased over the last three years. This is partly due to the addition of the Metro divisions. See Table III-8 for an exhibit of the loss rates.

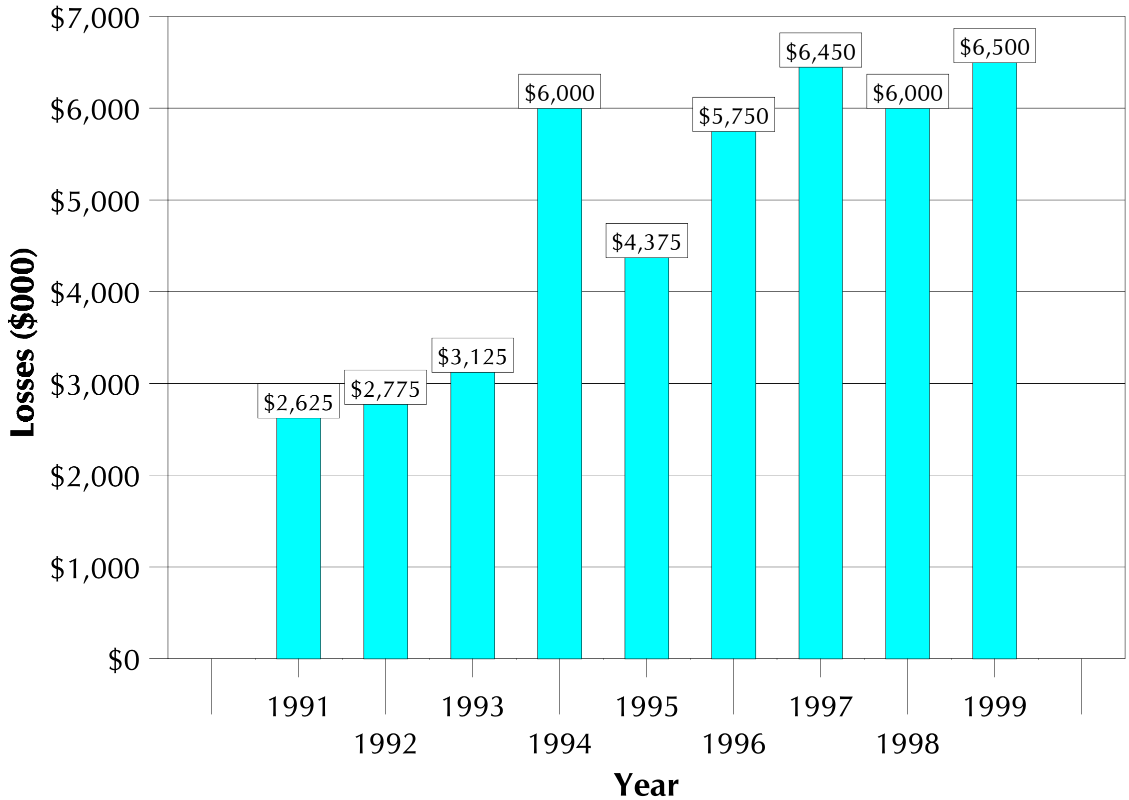
Table III-4
KING COUNTY
Workers Compensation
Projected Ultimate Incurred Losses*



*Data obtained from Fallquist actuarial study dated 9/3/98.

Table III-5 illustrates that general liability losses have been fairly steady over the past three years. See Table III-9 for loss rates.

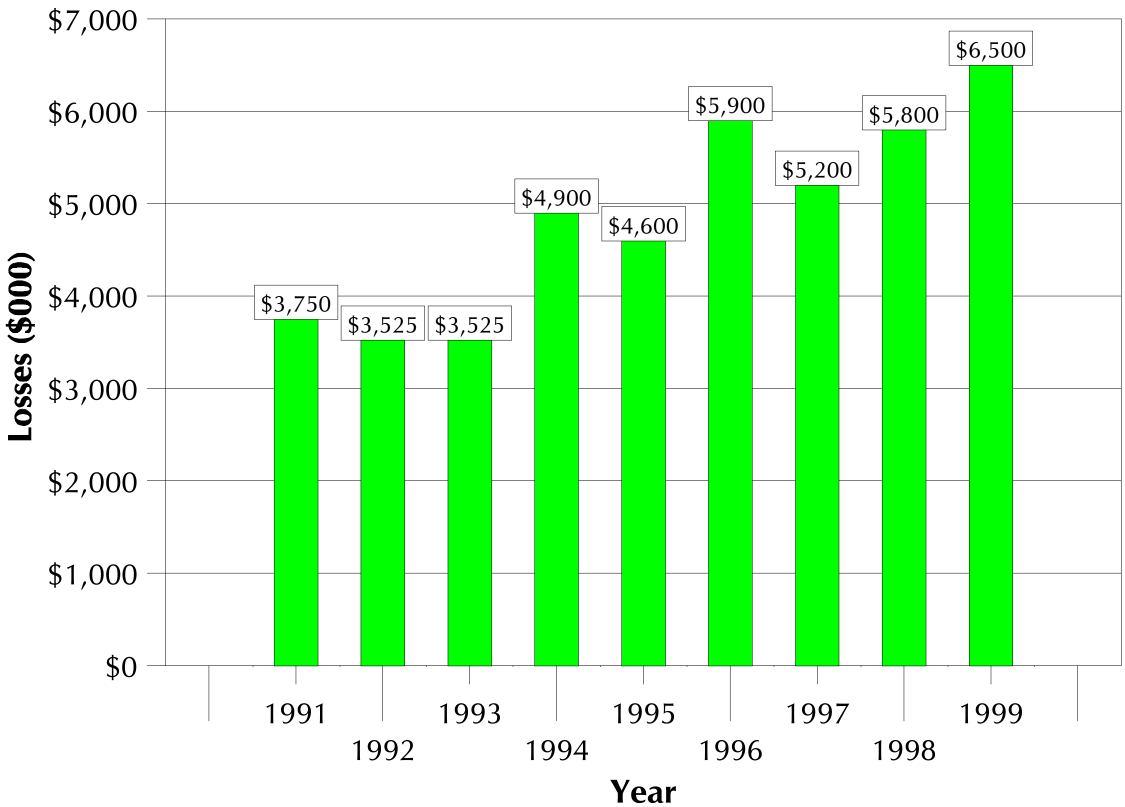
Table III-5
KING COUNTY
General Liability
Projected Ultimate Incurred Losses*



*Data obtained from Fallquist actuarial study dated 9/3/98.

Table III-6 illustrates that automobile liability losses have been fairly steady over the last three years. See Table III-10 for loss rates.

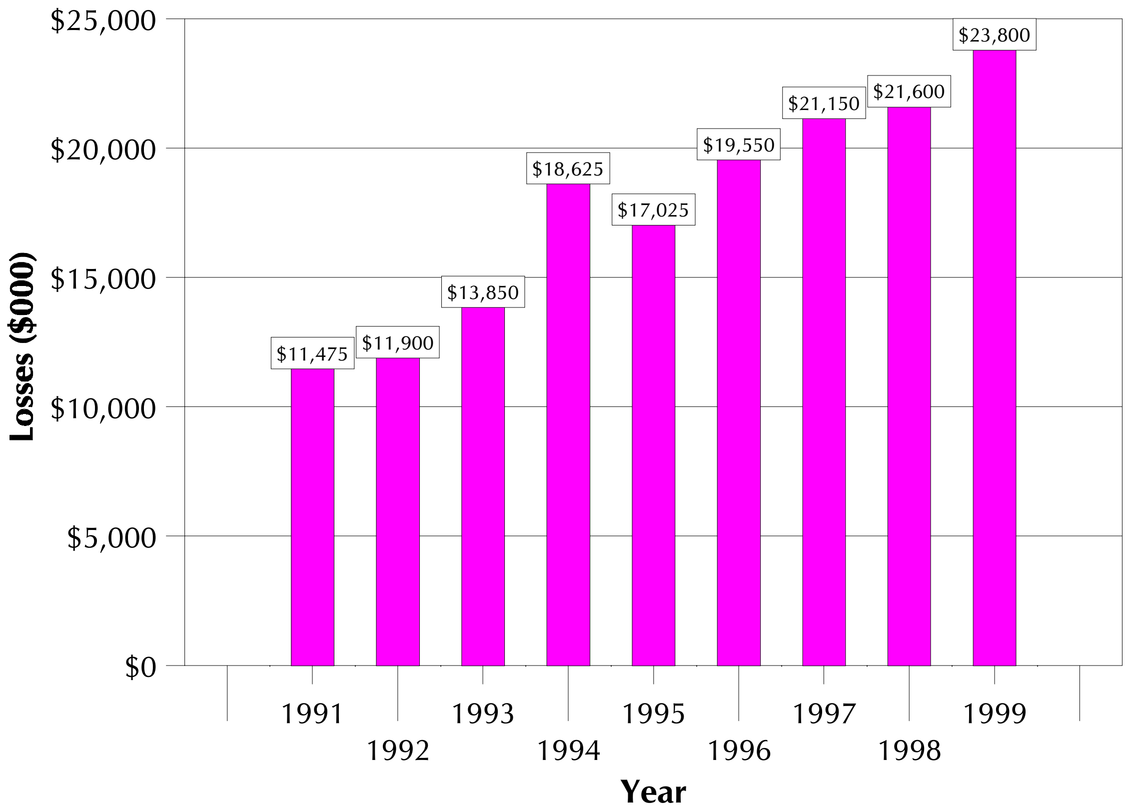
Table III-6
KING COUNTY
Automobile Liability
Projected Ultimate Incurred Losses*



*Data obtained from Fallquist actuarial study dated 9/3/98.

Table III-7 illustrates projected ultimate losses for workers compensation, general liability and automobile liability combined. See Table III-11 for loss rate history.

Table III-7
KING COUNTY
All Lines Combined*
Projected Ultimate Losses



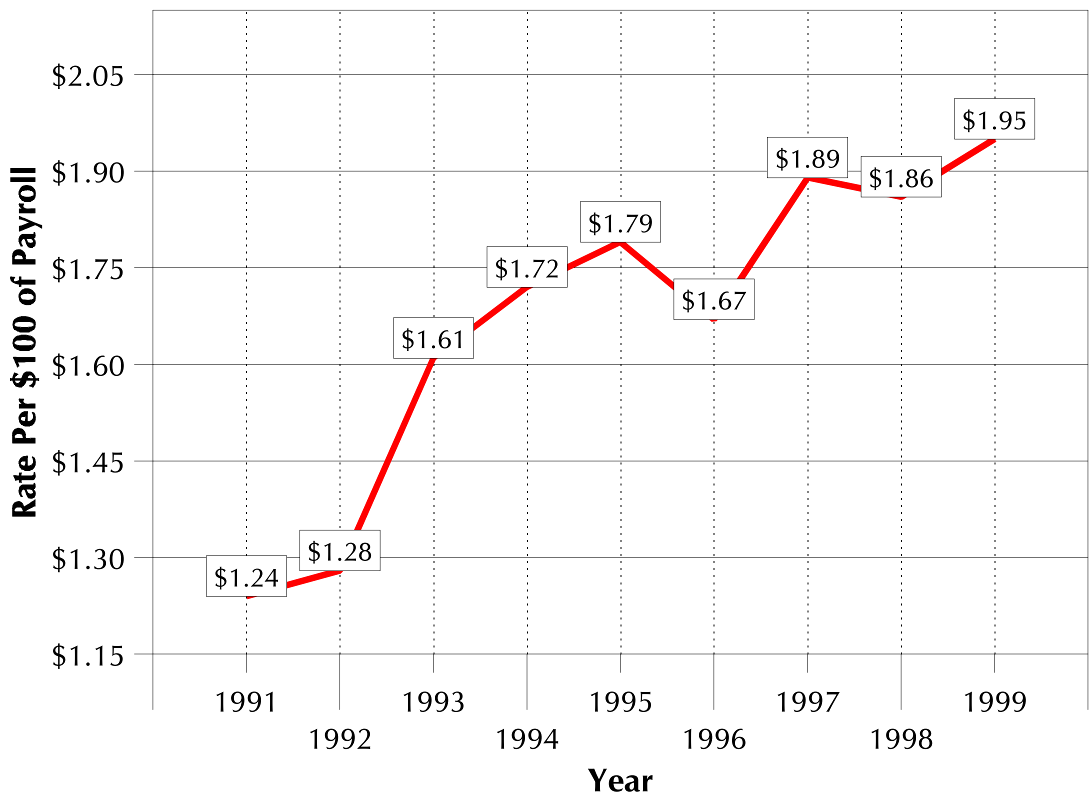
*Workers compensation, general liability and automobile liability.

C. LOSS RATES

Dividing losses by a pertinent exposure base develops a loss rate per unit of exposure. This measurement can be used to determine the true direction (or trend) of losses. For example, if projected ultimate losses increase by $1 million from one year to the next, but the loss rate stays the same, there has been no change (deterioration, in this case) in the rate of loss.

Table III-8 illustrates the loss rates for workers compensation. Except for slight dips in 1996 and 1998, the loss rate has increased every year since 1991.

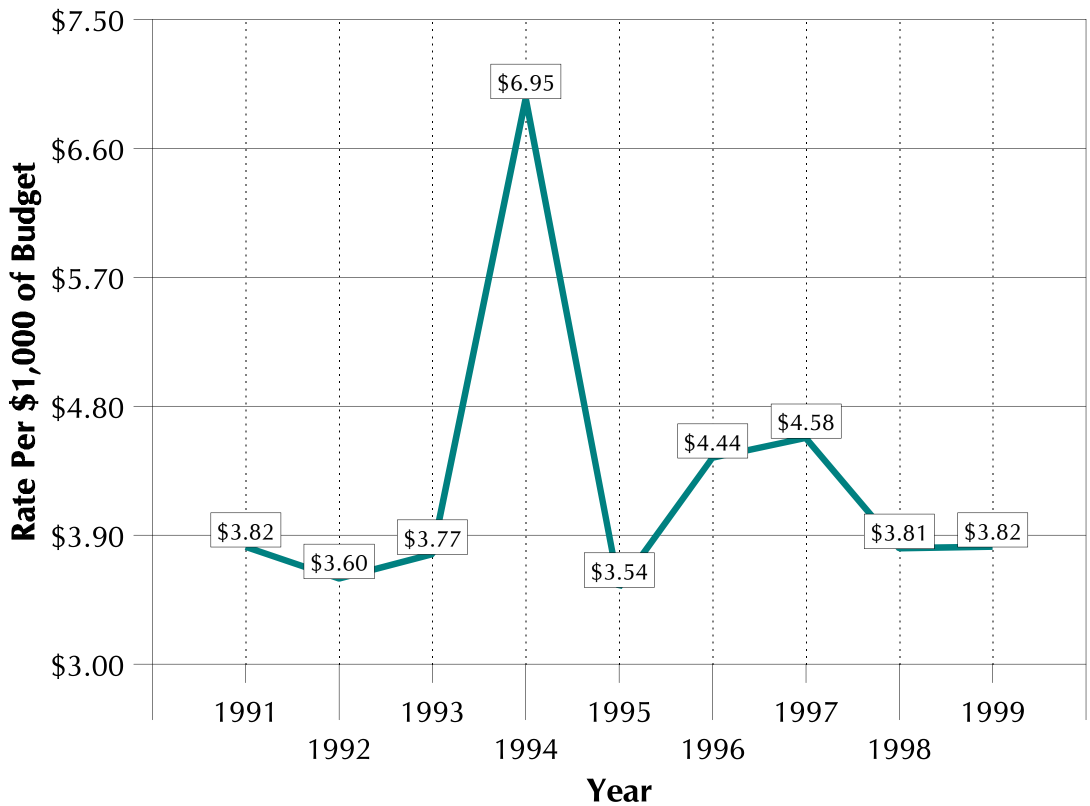
Table III-8
KING COUNTY
Workers Compensation Loss Rates*



*Loss data obtained from Fallquist actuarial study dated 9/3/98, payroll information obtained from Safety & Claims.

Table III-9 illustrates the loss rates for general liability. Other than a huge variance in 1994 (due to a large loss) and minor ones in 1996 and 1997, the loss rate has remained fairly steady since 1991. This confirms our positive evaluation of the County's loss control efforts in this category in Chapter V.

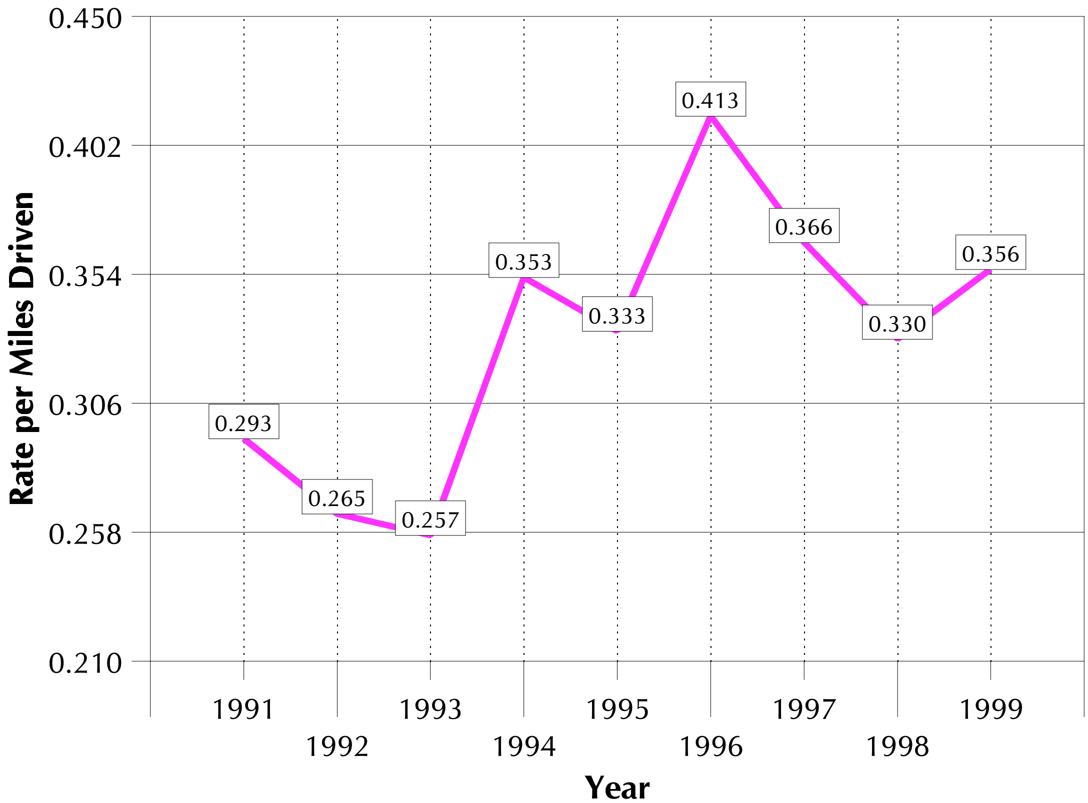
Table III-9
KING COUNTY
General Liability Loss Rates*



*Loss data obtained from Fallquist actuarial study dated 9/3/98, budget information obtained from 1999 King County budget report.

Table III-10 illustrates the loss rates for automobile liability. Other than a slight variance in 1996, the loss rate has remained fairly steady since 1994.

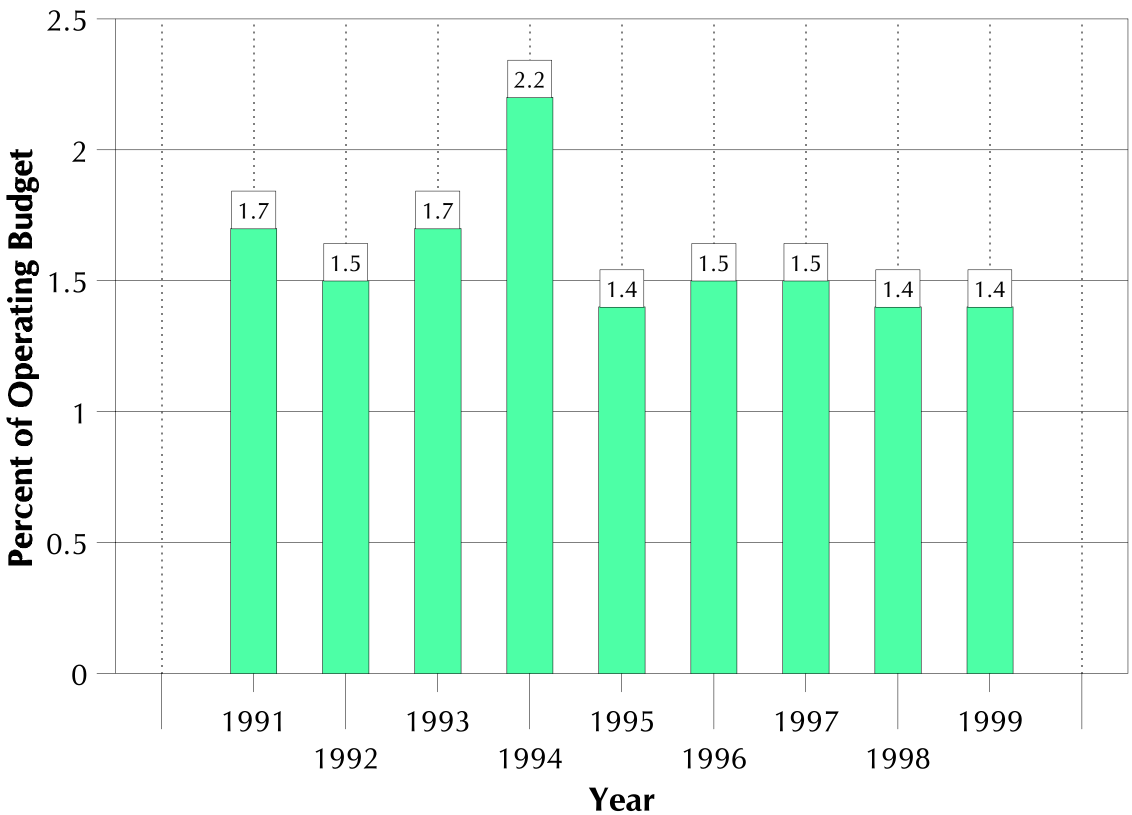
Table III-10
KING COUNTY
Automobile Liability Loss Rates*



*Loss data and miles driven obtained from Fallquist actuarial study dated 9/3/98 and Risk Management Division.

Table III-11 illustrates the loss rates for all three lines combined. This exhibit shows that, even though ultimate losses for all three lines are steadily rising (Table III-7), with the exception of 1994, the loss rate has remained between 1.4% and 1.7% of the operating budget. In fact, the loss rates for 1998 and 1999 are the lowest in the last nine years.

Table III-11
KING COUNTY
All Lines Combined*
Loss Rates



*Workers compensation, general liability and automobile liability.

- These statistics indicate that, overall, risk management policies and procedures have been effective. These numbers also support our interview findings that risk management is well received throughout the County and there are strong working relationships in place (see Chapter V). However, results need to be continually monitored to ensure that the County's risk management efforts remain effective.

D. BENCHMARKING

Table III-1 below compares an analysis of King County claim frequency and severity to similar statistics for seven California urban counties.

Table III-12
King County
California Urban Counties* Comparison

Claims Frequency and Severity	King County	California Urban Counties	
		Median	Range
Liability			
• Number of claims per 10,000 population	26.0	5.5	2.3 - 9.1
• Losses per 1,000 population	$7,083	$5,344	$1,195 - $7,305
• Average claim cost	$2,715	$7,366	$2,789 - $23,729
Workers Compensation			
• Number of claims per 100 employees	13.2	15.1	9.63 - 19.97
• Losses per $100 of payroll	$1.86	$2.36	$1.41 - $2.96
• Average claim cost	$5,613	$5,660	$4,732 - $7,578

- From data on seven California counties in an urban environment during 1991-1996 by CSAC-EIA and CIPRA.

1. Liability

The number of claims and losses per 1,000 population are much higher for the County than the California urban counties. The difference is probably because the County has a Transit Division and the California counties do not. By their nature, Transit Division operations generate a higher frequency of accidents, which causes both the number of claims and total losses paid to be higher than the California counties. Conversely, Transit Division claims are generally smaller than other types of liability claims and this factor provides an average claim cost for King County that is much lower than the California counties.

2. Workers Compensation

King County compares favorably to the California counties in all categories. The number of claims per 100 employees, losses per $100 of payroll and average claim cost are all lower than the median for California counties. King County's losses per $100 of payroll and average claim cost are even more impressive when taking into consideration the fact that King County's disability benefits are 40% higher than California's.

IV. RISK MANAGEMENT ORGANIZATION

The previous chapter tabulated the County's costs for risks of accidental loss arising from:

- Liability for injuries or damages to the public (liability).
- Obligations for medical costs and disability payments arising from on-the-job injuries to employees (workers compensation).
- Damage to County-owned property.

This chapter describes the County's organizational structure as it pertains to managing risk, the tasks performed and support systems that are in place to help the County manage its risks and the quality and extent of broker services received by the County to assist in the risk management process. Subsequent chapters review the effectiveness of the County's loss control efforts, claims management and processing, and risk financing decisions.

A. CURRENT STRUCTURE

Chapter 4.12 of the *King County Code* specified the scope of risk management for property and liability for the County. This legislation describes:

- Duties of the risk manager.
- Creation, composition and duties of the Risk Management Committee.
- Role and duties of the prosecuting attorney.
- Duties of county officers, employees and authorized agents.
- Procedures for handling claims and lawsuits.
- Defense of county officers, employees and authorized agents.
- Actions for recovery of losses.

Chapter 2.92 of the *King County Code* establishes the office of Safety & Workmen's Compensation Administration (later changed to Safety & Claims) and defines the responsibilities of the office.

Table IV-1 below outlines the division of duties for the three program areas of liability, workers compensation and property.

Table IV-1
Risk Management
Areas of Responsibility

Risk Management Discipline	Liability	Workers Compensation	Property
Program Management	RM	S&C	RM
Loss Control	RM	S&C	RM
Claims Management	RM	S&C	RM
Legal Defense	PA	PA	N/A
Risk Financing	RM	RM/S&C*	RM

RM = Risk Management **PA** = Prosecuting Attorney
S&C = Safety & Claims **N/A** = Not applicable

* **RM** sets the retention level and buys the excess insurance;
S&C determines Insurance Fund charges.

The division of duties described in the table above is appropriate and effective because:

- It gives each program manager responsibility and authority for all major risk management disciplines.
- It centralizes program fiscal responsibility.
- It incorporates necessary technical skills into each program.

Although they have separate areas of responsibility, Risk Management and Safety & Claims have overlapping areas of loss control. Hazardous activities at County facilities could impact both the public and its employees. These two divisions should meet regularly. This would promote a more synergistic approach to risk management, where problem solving resources could be deployed together to solve common problems.

The proposed cooperation could result in more complete solutions to identify problems and maybe more efficient deployment in staff, resulting in lower long-term staffing needs for the two divisions. While we would expect such cooperation to produce lower costs, there are too many variables to allow us to place a precise value on the savings that might result.

- We recommend that the Managers of Risk Management and Safety & Claims meet regularly to discuss common exposures and loss control measures.

1. Scope of Authority

The County's approach to risk management has changed since the last audit was performed in 1986. As the size and scope of the County's operations have grown over the last 13 years, so has the risk management function.

The insurance funds have grown from $3 million in 1986 to over $50 million in 1999. Liability coverage went from being unavailable at a reasonable price to the point where the County now has $100 million of affordable insurance limits in excess of it's $2.5 million retention. In 1986, 16 property and liability policies were purchased at a total premium of about $725,000. Today, 29 policies are in place with premiums in excess of $2.5 million.

The cost of risk has grown from around $8 million to around $30 million. It is interesting to note that the cost of risk as a percentage of the operating budget is about the same today as it was in 1986. However, this doesn't mean that the County can sit back and relax. With the County's high retention levels, risk costs can fluctuate dramatically and a run of workers' compensation claims or serious liability claims can quickly escalate the costs. In fact, more time and attention is needed today to deal with the increasing complexity of loss control challenges and keep the cost of risk at a stable level.

In 1986, a Risk Management Committee had broad authority for administration of risk management. The Committee was comprised of the Risk Manager, Chief Civil Deputy Prosecuting Attorney, Budget Division Manager and the Safety & Claims Manager. The committee composition remains, although the Risk Manager is now the Chair. Appropriately, the emphasis and authority for managing risk has shifted from the Committee to County staff members. The Committee now acts in a coordination and advisory capacity. This change is a major improvement. An entity as large as the County with its many diverse operations, needs full-time risk management professionals empowered to truly manage the County's risks.

The Safety & Claims Manager is a non-voting member of the Risk Management Committee. The County's annual workers compensation cost is about $12 million, or 40% of the County's total cost of risk. County facilities and operations where risk of loss to employees is present also impact the public. Many common issues exist in managing liability, property and workers compensation risks. Responsibility for the workers compensation concerns is with the Safety & Claims Manager, who has the responsibility to seek the most efficient means of addressing the concerns.

- We recommend that the Safety & Claims Manager be included as a voting member of the Risk Management Committee to promote a level playing field in the development of county-wide solutions to risk problems of all types.

2. <u>Placement</u>

Risk Management is a division of the Information and Administrative Services Department, which is one of thirteen County departments. Safety & Claims is a division of the Office of Human Resource Management Department and part of the County Executive office. Exhibit IV-1 displays where each of these units involved with risk are in the County's organization.

Risk Management manages all risks of property and liability loss emanating from all departments. Risk Management is also charged with managing County resources to buy insurance, to pay liability losses and to protect the public and the County's property via loss prevention activities. Furthermore, *King County Code* requires the Risk Manager to report insurance purchased, claim activity, insurance fund accounting and the level of retained risk to the County Council on a semi-annual basis.

The current placement of Risk Management does not prevent it from accomplishing its objectives. However, we feel Risk Management would have better visibility if it was moved from a line department to an area that is recognized for providing broad general services. We believe a better long-term placement would be in the County Executive office. This change to a higher level within the County will also create a perception of Risk Management as having stronger authority to accomplish its objectives.

- We recommend that Risk Management should be made part of the County Executive office (see Exhibit IV-2).

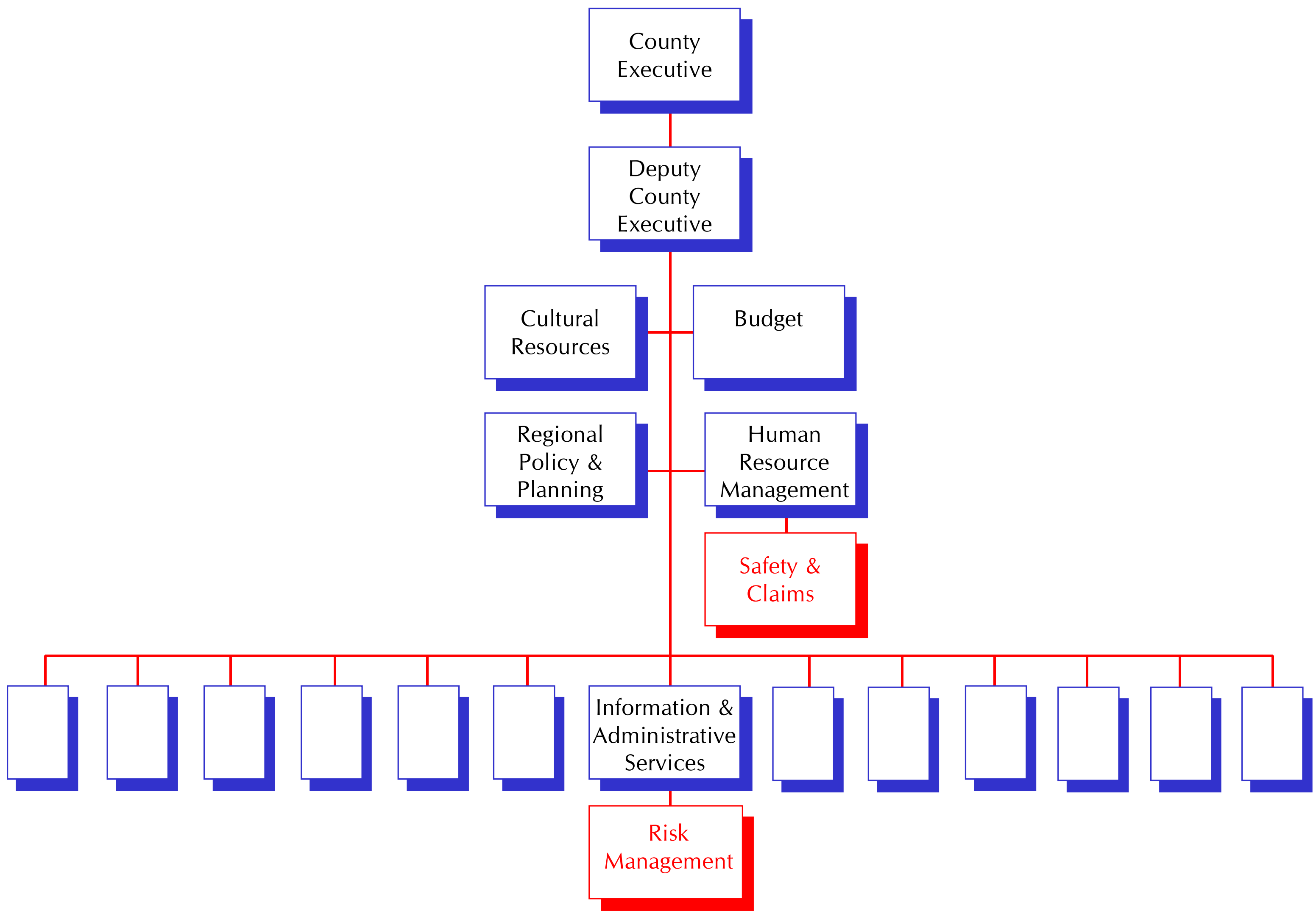
Safety & Claims provides services to all who are the County's human resources. Therefore, it is appropriate that Safety & Claims is a division of the Office of Human Resource Management.

3. <u>Roles and Activities</u>

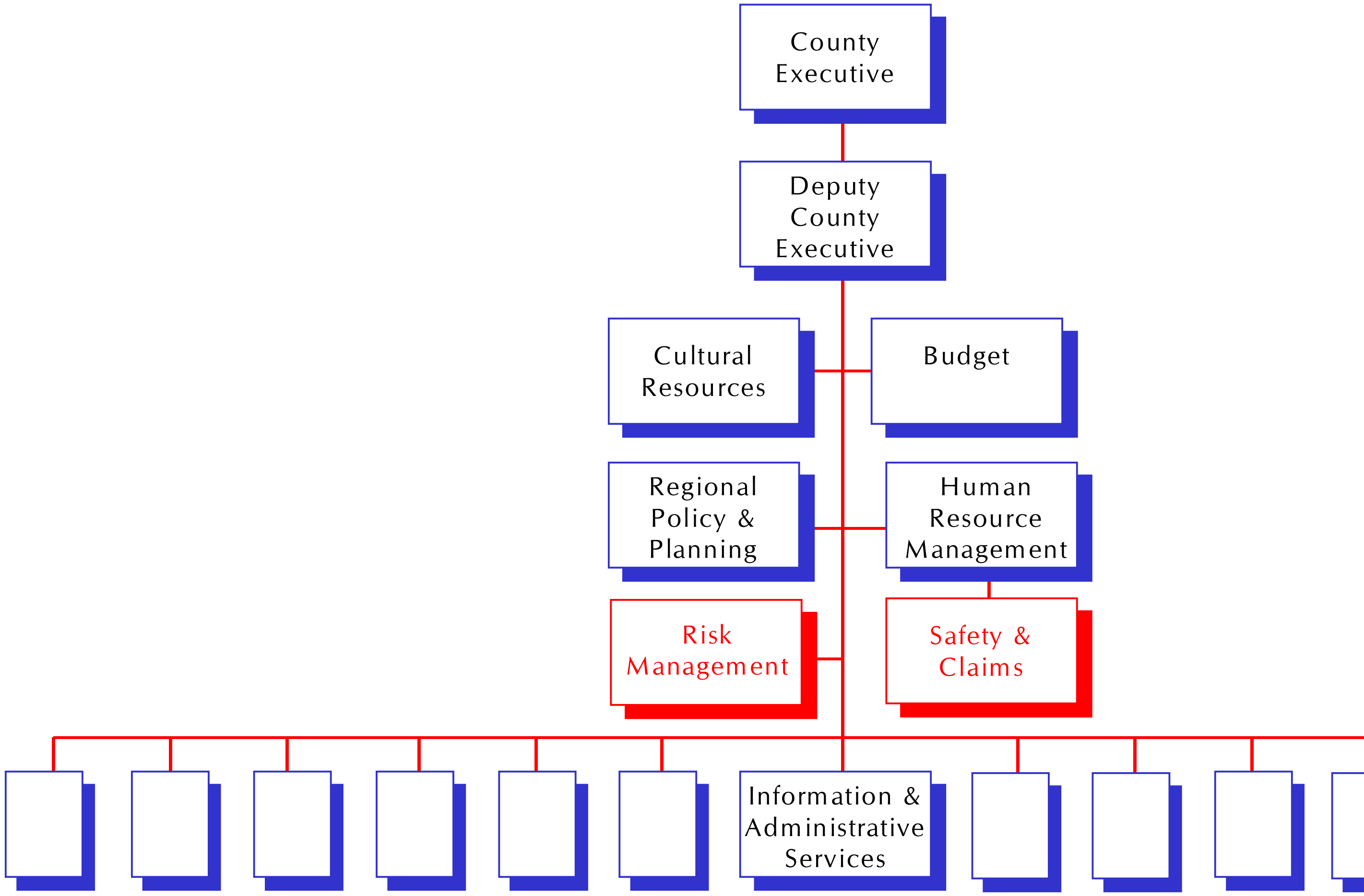
From our interviews and visits, we learned that the Risk Management Division is to be commended for its operations. There is a high regard among department directors and division managers for the Risk Manager and his staff. Communication flows strongly between Risk Management and the other departments. There is a great deal of respect among all parties. Without this rapport, the County's risk management process would not be effective.

Exhibit IV-1

KING COUNTY
Organizational Chart



KING COUNTY
Proposed Organizational Chart



The interview process also developed input that, until recently, the Safety & Claims Division was under-serving the County in handling claims. This situation changed with the prudent hiring of an experienced manager. Claims review meetings are being held on a regular basis, communication with department heads has increased, Safety & Claims officers have been assigned to specific departments, and supervisor training seminars have been initiated. Improvements are also being made in the areas of structure and personnel responsibilities, staff training, space planning, technological advancements, safety projects, return-to-work programs, revised allocation programs, distribution of data, automated telephone answering menu and performance measurements for staff members.

The Deputy Risk Manager purchases the excess workers compensation insurance and then communicates this decision to the Safety & Claims Manager. Since the premium for this coverage is an element of the cost of risk for workers compensation, it would be more appropriate if the input of the Safety & Claims Manager was obtained prior to coverage being purchased.

- We recommend that the Safety & Claims Manager be involved in the analysis and decision-making process regarding the purchase of excess workers compensation policies.

4. Staffing

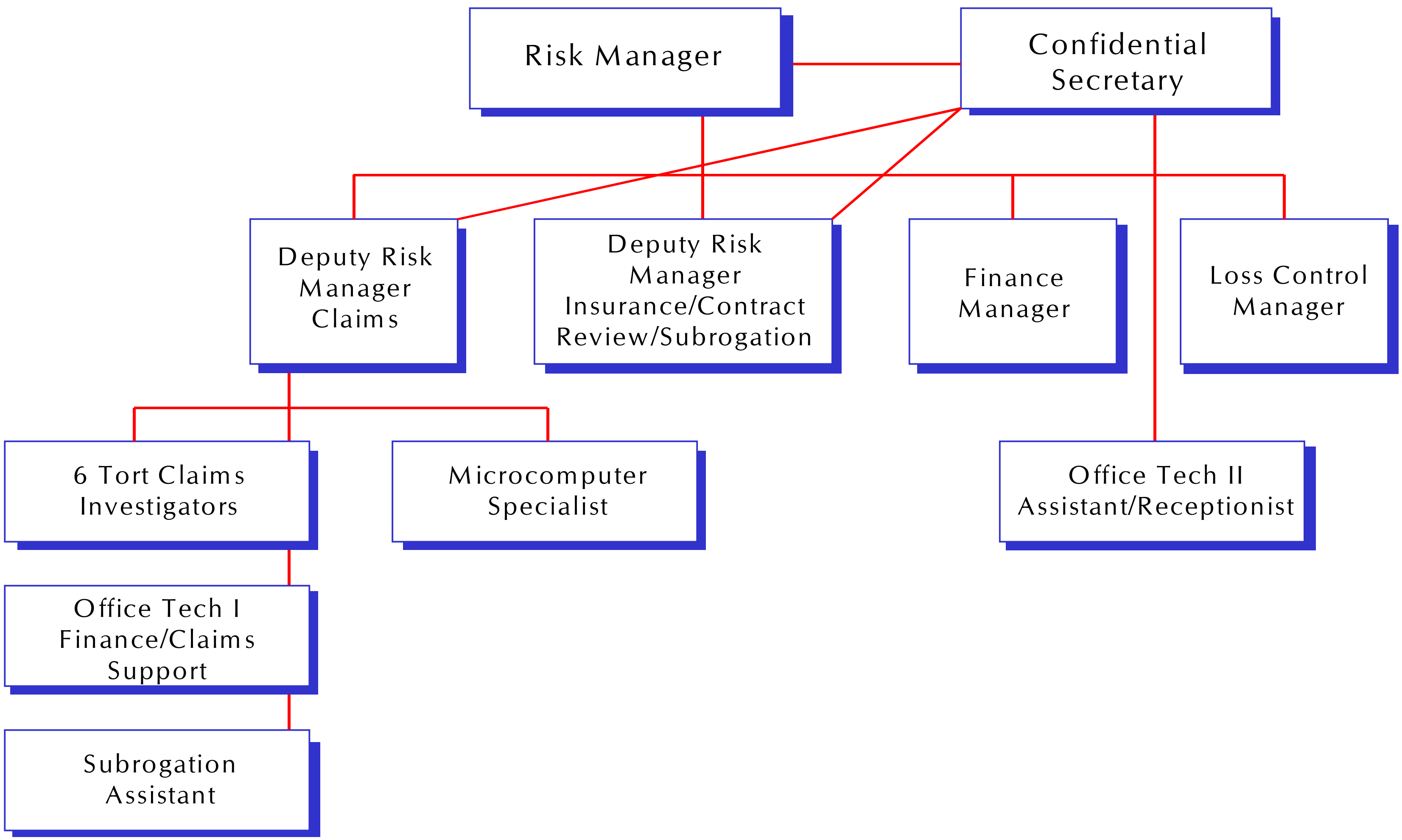
Exhibit IV-3 illustrates the staffing and organizational structure of the Risk Management Division. The department includes a Risk Manager, Deputy Risk Manager, Finance Manager, Loss Control Manager, an Office Technician and a Secretary. The remaining members of the department are claims personnel. The analysis of claims staffing is in Chapter IV, "Claims Administration & Management."

The Risk Manager has added a Finance Manager to coordinate the annual allocation of property and liability costs to departments and other pertinent financial matters. A Loss Control Manager has also been added to assist in the development and oversight of loss control activities. These positions are necessary for Risk Management to effectively manage risk. The addition of these staff members will keep the Risk Manager from getting immersed in technical detail. It will give him more time to manage program results and to identify and meet specific needs of department directors.

The primary duties of the Deputy Risk Manager include contract review, insurance administration, loss control, training other departments about certificates of insurance and to provide assistance to the Risk Manager.

Exhibit IV-3

KING COUNTY
Risk Management Department Organization Chart



Risk Management also utilizes the services of two consultants on a part-time basis. One consultant reviews insurance and indemnity provisions of actual and proposed contracts entered into by the County. The same person also evaluates insurance policy provisions and endorsements of the County's contractors to assess if adequate coverage is provided. The other consultant provides property loss control support. Both of these positions could be staffed in-house, but consultants were chosen in order to meet W/MBE requirements.

Risk Management structures and responsibilities vary from entity to entity. There is no clear standard for staffing the function. We use experience-based judgment to evaluate staffing levels after reviewing duties, responsibilities and results.

With the Risk Management staff that is currently in place at the County, all necessary tasks that are described in the next section of this chapter are being performed. These include the following:

- Communication
- Reports
- Risk Cost Allocation
- Risk Management Information System
- Risk Identification
- Contractual Risk Transfer
- Loss Control (Chapter V)

Based on our analysis of the effectiveness of these tasks being performed, the County's cost of risk and loss rates, and the recent additions to staff, we judge that the Risk Management Division is adequately staffed.

The analysis of Safety & Claims staffing is included in Chapter VI, "Claims Administration And Management."

B. TASKS AND SUPPORT SYSTEMS

Risk costs flow from the facilities and operations. A risk manager has virtually no control over the factors that generate most risk costs — operating managers do.

To control risk costs, the Risk Manager (and, in the case of the County, the Safety & Claims Manager) must coordinate with those in operating departments and define roles and responsibilities. It is also important to provide feedback on results so that each department can see the results of their efforts.

To achieve these goals, a Risk Manager must be an effective communicator, both orally and in writing. The foundation for this process is a reliable risk management information system (RMIS).

1. Communication

There is a great deal of communication between the Risk Management Division and other County departments. This involves discussions of events, activities or changes within a department and their impact on risks and loss exposures. Risk Management also works closely with the Prosecuting Attorney Office to assist in the settlement of claims and to learn of trends in litigation. As mentioned above, the Risk Manager chairs the Risk Management Committee, advises its members and seeks Committee approval for various Risk Management activities.

In the past, there was very little communication between Safety & Claims and the departments regarding workers compensation claims processing. Sometimes an employee would go on disability and return to their job a year later without the department head receiving prior notice. However, this situation is now rectified. The new Safety & Claims Manager holds regular claims review meetings with departments. The Manager has also increased other communications with department heads.

2. Reports

The Risk Manager submits a report to the County Council on a semi-annual basis. The report summarizes claims activity, insurance fund transactions and insurance purchases for the prior year. These reports satisfy the requirements included in Chapter 4.12 of the *King County Code*.

We see the need for the Risk Management division to prepare an annual report designed for the County Executive and the department managers. This report would include a cost of risk tabulation (see Table III-1) for the most recent year and the prior four years for comparison. The cost would be presented as a total dollar amount as well as a percentage of the respective year's operating budget or some other basis for comparison. Tracking this information would provide the County with a measure of the effectiveness of its risk management program. If the cost of risk increases, the County can do further analysis to find out why and where changes are needed to its risk management strategies and tactics to respond. Communicating the annual cost of risk to the department managers will, with additional detail by department, highlight the extent of the County's expenditures for self-insured losses and the need for department commitment to loss control.

Other information to be included in the report is liability claim frequency by department (for each of the last five years) compared to the changes in departmental operating budgets and miles driven for general liability and automobile liability, respectively. Such comparisons will indicate whether the changes in claim frequency are due to changes in exposures, improvement or deterioration of loss control, or some combination of both.

A few paragraphs highlighting loss control efforts for the prior year and those proposed for the upcoming years would again focus the spotlight on the need for effective County-wide loss control.

- We recommend that Risk Management prepare an annual report for the County Executive and department managers that would include County-wide cost of risk, claim frequency and loss control information.

Safety & Claims publishes an annual report that is sent to all departments and to the County Executive. It provides a review of workers compensation claims, statistics, injury prevention activities and a written summary of the claims activity for each department. In addition to providing claims counts, it also compares frequency rates per 100 workers as well as average claim costs for the prior two years for each department. These statistics are very meaningful in helping each department determine the effectiveness of their loss control efforts. Overall, the report is a valuable communications tool and is a much-needed improvement by Safety & Claims in this area.

3. Risk Cost Allocation

The Risk Management Division develops an annual report detailing the amount each department will contribute to liability and property risk costs. Such funds flow to the Internal Service Fund for Insurance. Premiums are allocated based on each department's exposures compared to the total exposure for the County. This makes sense. Losses are allocated based on each department's loss experience for the prior ten years as compared to the County's total for the same period. Allocating losses in this manner does not reward or penalize the departments quickly enough for the effectiveness of loss control.

- We recommend that Risk Management use no more than the most recent five years of loss experience to calculate each department's loss allocations.

The proposed allocations are based, in part, on the actuarial report which is released in late August or early September. Because of this timing, departments do not see their proposed Insurance Fund charges until early October. The budget is usually finalized by late November. This does not leave much time to allow discussions with each department regarding their proposed contribution to the fund, and make any changes, if necessary.

- We recommend that Risk Management contract to have the actuarial report released by August 1 of each year and prepare and distribute suggested premium and loss allocations no later than September 1 of each year.

Safety & Claims allocates workers compensation losses to the departments. It does this by utilizing the most recent five years of loss data County-wide for the respective job classification. A "rate per hours worked" is then determined for each class code. This factor is then applied to the number of hours worked for each type of employee for each department. Current methodology does not allow a particular department's good or bad loss experience to impact its contribution rate. All departments pay the same rate for similarly classified employees.

- We recommend that a factor based on each department's loss experience be applied to the rate used to allocate workers compensation losses when calculating loss allocations.

4. Risk Management Information System (RMIS)

Risk Management is responsible for the handling of 4,000 liability claims and incidents each year. It has been managing these claims and other risk management information with a combination of a manual process and an automated database program. The software is not Y2K compliant. However, Risk Management has purchased an RMIS that will computerize the process and convert their data to a Y2K compliant system. It will also convert Transit claims data (handled by Crawford & Company) to the new RMIS. This will allow Risk Management to perform the same loss control and financial analyses on Transit claims as it does on claims incurred by other departments. The RMIS will also increase the speed and efficiency of claims handling done by Risk Management and there will be better integration of tort claims investigation work because the Prosecutor's Office will have RMIS workstations.

- We recommend that Risk Management convert to the new RMIS as soon as possible to enhance their claims handling and risk management information capabilities.

The RMIS used by Safety & Claims is the PARARISK system. It is adequate to produce meaningful loss control and exposure information.

5. Risk Identification

The key components of the risk management process are illustrated in Exhibit IV-4. The process begins with the identification of operations or aspects of an organization's activities that could lead to accidental losses. An entity must be aware of its exposures before it can determine how to address them. The process requires knowledge of facilities and operations, the types of indemnity/insurance clauses in all contracts, new activities underway or being planned in operating departments and litigation trends.

Property and liability exposures are identified by the Risk Manager with assistance from the Deputy Risk Manager. Activities regularly included:

- Site visits.
- Contract review.
- Response and evaluation to department contacts about potential exposures.
- Communication with the Prosecuting Attorney's Office regarding litigation trends and loss control.
- Analysis of each department's loss activity.

Risk financing plans have been designed to cover all major risks where it is fiscally sensible to do so. Staff knowledge of County exposures is excellent and efforts to control losses are sound. The Risk Management Division has tapped into the communications network at the County. We conclude that Risk Management has done an effective job in identifying risks.

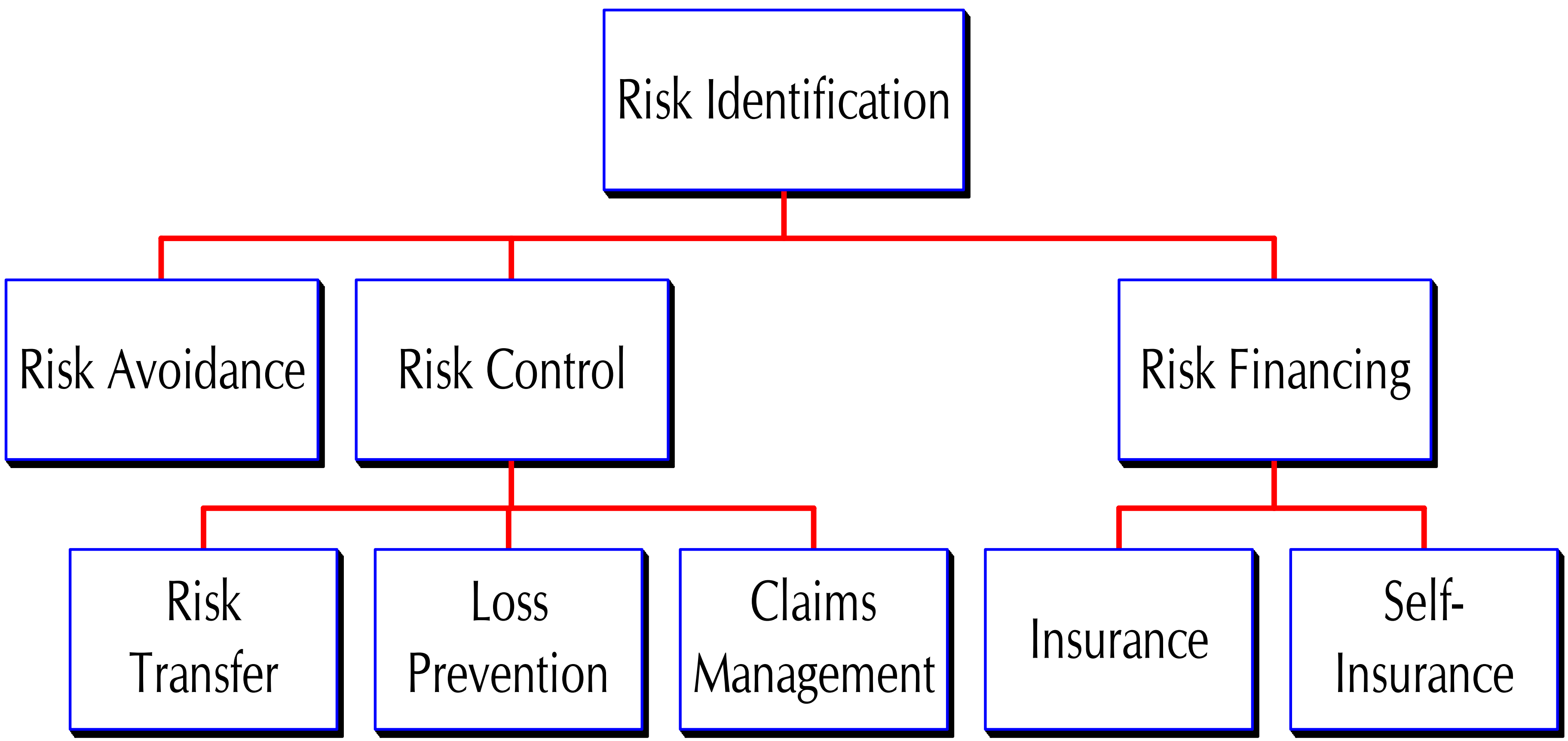
Workers compensation exposures are identified by the Safety & Health Supervisor and four Safety & Health Officers. This process includes:

- Assigning each officer to monitor and work with specific departments.
- Utilizing an industrial hygienist for ergonomic concerns.
- Analyzing loss data to identify cause and nature of injuries.
- Obtaining department manager feedback on safety concerns.

We judge that Safety & Claims is effectively identifying risks.

Exhibit IV-4

KING COUNTY
Risk Management Process



6. <u>Contractual Risk Transfer</u>

One method of dealing with risk is to contractually transfer it to another entity. This is done when effective insurance requirements and indemnity clauses are added to construction, maintenance and other contracts an entity enters.

The County insists on its preferred insurance and indemnification provisions in contracts. The Deputy Risk Manager develops and maintains the insurance and indemnification language for the County's standard contracts. The Deputy also supervises the review and negotiation process of these provisions and ensures compliance.

We have reviewed the documents and procedures that the Deputy Risk Manager has developed. While documents are technically sound, we have some concerns. The insurance requirement in the construction contracts seems unnecessarily limiting to the County. These contracts limit the contractor's liability insurance coverage to the County only to the extent of the contractor's negligence. We are aware that there is a State Statute that limits indemnifications to this extent, but are unaware of any provision that places a similar restriction on insurance coverage. Furthermore, insurers today are very willing to offer coverage for an owner's negligence exposure for losses associated with the contracted work.

- We recommend the County remove this limitation to the protection it receives from others' insurance.

Prior to contracts being awarded, Risk Management ensures that proper certificates are in place. However, it is the responsibility of each project manager to ensure that all necessary insurance policies are reviewed and replacement certificates are received.

- We recommend that Risk Management perform periodic audits to ensure that contract insurance requirements are being met. This would properly place the burden of this responsibility on personnel with technical insurance and/or risk management backgrounds.

The County's standard contract language extends insurance coverage requirements to subcontractors. While such wording offers improved protection of the County's interests, we think it's benefits do not exceed the effort it takes to monitor compliance. Further, regardless of whether subcontractors are asked to purchase insurance, the County is protected by the contractor's insurance coverage. Strongly monitoring contractors will sufficiently protect the County.

- We recommend discontinuing the practice of monitoring insurance from subcontractors.

C. BROKER SERVICES

The County relies on a broker to assist in the procurement and maintenance of its property, liability and workers compensation insurance policies and program. The broker's work includes:

- Exposure analysis.
- Providing marketing strategy.
- Drafting policy language and developing underwriting specs.
- Obtaining bids and negotiating best terms and coverage.
- Verifying policies and checking for accuracy and compliance to specs.
- Reviewing coverage issues as needed.
- Notification and tendering of losses.
- Administering notary and self-insured bonds.
- Providing related consulting services as needed.

Since 1992, the County has contracted with Willis Corroon (Willis) to provide the above services. Willis uses a strong account team experienced in the public sector to service the County. Meetings are held quarterly to discuss risk management program issues and provide updates on the broker's activities.

Willis assisted the County in designing the original liability program document and in obtaining subsequent enhancements. Since 1995, Willis has been successful in increasing the County's liability limits from $50 to $100 million while simultaneously obtaining premium decreases from $965,000 to $750,000. Property insurance was also recently renewed for a three-year term on June 1, with a premium reduction in excess of $400,000.

The County paid a fee of $138,300 for the services received from Willis during the 2/1/98 contract year. The fee includes compensation for subcontractors. After deducting the subcontractor charges, the direct compensation earned by Willis is $106,000. Compared to total insurance premium placed, the broker's fee is about 4%. This is less than half of the standard commission that a broker would earn if compensated on a commission basis.

- In our judgment, the County is receiving the quality and quantity of service necessary from its broker at a very reasonable cost.

V. LOSS CONTROL

This chapter examines the County's approach to loss control and the subsequent activities directed toward preventing liability, property and workers compensation losses and reducing the size of losses that do occur.

King County's mission is: "To enrich the social, economic and environmental vitality of the region by providing high-quality and responsive public services." The County does this when it offers its residents public transportation, parks and recreational facilities, treatment of wastewater and protection of its citizens and their property. However, all of these activities, as well as the other ones that the County provides, have elements of risk that could cause liability, workers compensation or property damage losses.

A. BALANCING OBJECTIVES

As its mission statement indicates, the County has chosen to offer its citizens a high degree of quality services. Although the County attempts to control losses, it realizes that risk remains in some operations or facilities. The only way to eliminate the risk is to terminate the operation or close the facility. The County has decided it is more important to have these services available to the public.

Examples of relatively high-risk activities include the skateboard park, climbing rock and velodrome. The County has properly posted signs warning that users do so at their own risk, restricted the hours of operation, built a fence around the climbing rock and regularly checks to ensure that the phone booth in the area is working in case of any emergencies. Despite these reasonable risk control measures, accidents will occur at these facilities. If they are severe enough, the County will get sued and could potentially pay large liability sums. To keep such operations and facilities open to the public requires analysis to find means to reduce loss potential.

B. COUNTY APPROACH

1. Liability and Property

The Risk Management Division is responsible for the County's property and liability loss control. Staffing for liability loss control includes the Risk Manager, Deputy Risk Manager and, recently, a Loss Control Manager. Transit, Wastewater, Water & Land, Roads, Sheriff and Parks all have safety personnel on staff. Transit has twelve and Wastewater has four. Other County departments have individuals who coordinate loss control activities with Risk Management, but who have other duties as well.

Now that the Risk Management Division has a Loss Control Manager, group meetings with all County personnel responsible for loss control will be held at least twice a year. Meetings will also be held on an individual basis to determine the greatest needs of each department.

Liability risk control activities include the following:

- Site visits and facility inspections.

- Review of contracts to assure contractors (and others the County does business with) have adequate insurance.

- Communications with departments regarding upcoming activities or planned changes to operations or facilities.

- Analysis of loss data, to identify adverse trends and develop methods to keep claims from reoccurring.

- Communication and advice from the Prosecuting Attorney's office regarding statutory changes, court cases that redefine duties and suggested procedural changes to reduce the County's liability expenses.

Property loss control is provided by the Deputy Risk Manager, who is a credentialed fire protection engineer, a consultant and the property insurer. The insurer spends 1,000 hours per year performing inspections, construction plan review and testing protection systems at the County's facilities. The cost is included in the premium and is part of the insurer's overhead expense. The consultant visits the sites to ensure compliance to the insurer's recommendations.

- Based on activities performed and loss history, the County has sufficient personnel in place in Risk Management and throughout the various departments to effectively handle the liability and property loss control.

According to Chapter 4.12.030 of the *King County Code*, "The Risk Manager shall advise all county departments, divisions, and other county agencies regarding risk management and reduction of risk and exposure to loss, including programs and precautions for safety to reduce hazards to the public that may exist in county facilities and operations." Since it is charged with this responsibility, it is appropriate that Risk Management have an active leadership role in directing, coordinating and monitoring countywide loss prevention activities.

A loss control contingency fund, which is used for special loss control needs of operating departments and divisions, provides Risk Management with a resource to help its loss prevention responsibilities. We think the fund is a good tool. It provides funds to address an immediate loss control need without upsetting the operating department/division budget.

Prior to 1999, the annual fund amount was $35,000. It was fully utilized each year. The fund has since been increased to $100,000. This amount will be fully expended this year. Whatever amount is placed in the fund can readily be used to address the County's safety needs. Additional funding will allow Risk Management to have an even greater impact in the area of loss prevention. Examples of areas Risk Management could apply these funds to include:

- Upgrading loss control at the Factoria Waste Transfer Station and others of similar construction. This facility has open pits that people could quite easily fall into and suffer severe injuries when dumping their waste. The contingency fund could be used to provide signs, retaining walls, and loss control inspections.

- Supplement training funds for the Sheriff's Department to ensure that all officers receive reinforcement in the proper use of force, defensive and emergency driving techniques and biohazard exposures.

Unlike Risk Management, Safety & Claims does not have a loss control contingency fund at its disposal. However, Safety & Claims does have a similar responsibility for controlling losses. If Safety & Claims had a contingency fund, it, too, would be able to adopt a more active leadership role in controlling losses.

We believe that the loss control contingency fund should be increased to assist in controlling both liability and workers compensation loss exposures. There are no generally accepted guidelines for establishing amounts in funds like this. However, we judge 1% of the cost of risk, or $300,000, to be a reasonable budget for County loss control activities. The funds would be shared by both Risk Management and Safety & Claims. The usage and amounts would be determined at the time of need by the Risk Management Committee.

- We recommend that the loss control contingency fund should be increased to $300,000. It should be used for both liability and workers compensation needs and jointly funded by the two programs.

2. Workers Compensation

Safety & Claims staffs the loss control function for workers compensation with four safety officers and one training officer. The officers are assigned to specific departments, allowing them to concentrate their efforts and customize their services. Inspections and safety meetings with departments are regular. Accident prevention programs are in place.

An industrial hygienist performs ergonomic studies. Loss data is analyzed to determine reoccurring loss causes and the nature of claims.

Transit has a safety officer assigned to each of six bases. Drivers are trained in defensive driving and first aid. Maintenance personnel are trained in hazard communication. Mechanics who work around the trolleys or the electrical substations receive electrical training. Because of the unions, safety meetings are voluntary or employees have to be paid to attend. Triennial audits of the operation are performed by the Federal Transit Administration. These audits include a safety component, in which the County is measured against minimum standards.

Wastewater and parts of Water & Land, which were former Metro divisions, also have their own safety staff. Four safety officers handle the loss prevention function and are partly responsible for successfully reducing by 27% the number of claims filed from 1997 to 1998.

- Based on activities performed and loss history, the County has an adequate number of safety and loss control employees to address its workers compensation exposures.

Other than initial claims investigation and coordination, there is little communication and coordination of safety and loss control activities by Transit and Wastewater with Safety & Claims. Initially, after these divisions merged with King County, meetings were held on a regular basis. However, this is no longer the case. Ongoing communication would lead to a greater synergy within the respective safety groups and provide an awareness and better use of available County resources in this areas.

- We recommend that safety personnel from the former Metro divisions and Safety & Claims meet regularly.

C. EMPLOYMENT PRACTICES

This area of liability exposure is the fastest growing source of claims in the Country. Some public employers report 40% of all new liability claims have employment practices allegations.

The County is concerned that its employees are treated fairly. An Employment Practices Oversight Committee (the Committee) has been established. Its duties are to provide strategy guidance for dealing with difficult employment cases and to act as a policy group in addressing emerging issues. The Director of the Office of Human Resource Management is responsible for implementing and monitoring policy and procedural changes developed by the Committee.

While the above measures are worthwhile, additional procedures should be considered to prevent losses as well as strenghten the County's defense. As recently as 1998, the U.S. Supreme Count found that an employer can avoid liability if it can prove (1) that it "exercised reasonable care to prevent and correct promptly any sexually harassing behavior" and (2) that the complaining employee "unreasonably failed to take advantage of any preventive or corrective opportunities provided by the employer or to avoid harm otherwise."

Although supervisor training is available, we learned through our interview process it is not routinely received. We understand a department's workload frequently takes precedence over training newly promoted supervisors. A lack of supervisory training makes the County an even bigger target for such claims and weakens the first defense mentioned in the paragraph above.

- We recommend that supervisor training on employment practices be evaluated for compliance and strengthened.

If an employee feels that discrimination has occurred in their department, there are several formal avenues within the County to lodge a complaint. However, according to expert witness testimony provided by Dr. Freada Klein in Snider v. Consolidation Coal Company, "95% of the victims of nonconsensual relationships do not complain or report the wrongdoing because of fear of reprisal or loss of privacy." A solution to this concern would be the usage of an outside source that utilized an "800 hotline" phone service to protect employees' privacy. The outside service would then contact an individual at the County responsible for investigating such claims. This method would allow the County the ability to protect the employee's privacy, the opportunity to investigate and possibly correct a situation before it evolves into an actual claim and provide employees with another "preventive or corrective opportunity" (which further strenghthens the County's defenses).

- We recommend that the County use an outside service for reporting of discrimination concerns by employees. An in-house position should also be established with responsibility for investigating such situations and working with the Committee to determine corrective action, if necessary.

VI. CLAIMS ADMINISTRATION AND MANAGEMENT

This chapter of the report summarizes the results of our evaluation of the workers compensation and liability claims handling practices of the County. The on-site analysis was conducted 2/22/99 - 3/17/99 at various County locations. This element of the project includes:

1. Review of 106 workers compensation claims. The category of claims and the number of claims reviewed for each category are:
   - 75 open indemnity (lost time)
   - 17 closed indemnity
   - 14 medical only
2. Sixty-one (61) non-Metro liability claims. The category of non-Metro claims and the number for each category are:
   - 33 open files at Risk Management Office
   - 28 closed files at Risk Management Office
3. Seventy-one (71) Metro claims reviewed at Crawford & Co. (Crawford) in Bellevue.
4. Sixteen (16) liability files reviewed at the Prosecuting Attorney Office (Civil Division — Tort Section). Eight of these files were Metro claims and 8 were non-Metro claims.
5. Discussions with the following County personnel:
   - Manager — Safety and Claims (workers compensation)
   - Former Claims Supervisor (workers compensation)
   - Two Claims Officers (workers compensation)
   - Assistant Chief Civil Deputy — Civil Division, Tort Section, Prosecuting Attorney Office (Metro and non-Metro)
   - Two Deputy Prosecuting Attorneys (Metro and non-Metro)

- Tort Investigator — Prosecuting Attorney Office
- County Risk Manager
- County Deputy Risk Manager — Claims

3. Discussions with the following personnel at Crawford:

   - Branch Manager
   - Casualty Adjustor assigned to County claims

4. Follow-up discussions with the County and Crawford Personnel.

A. WORKERS COMPENSATION CLAIMS MANAGEMENT ANALYSIS

1. Technical Categories

a. Staffing/Caseloads

Exhibit VI-1 on page 46 displays the organizational makeup of the County workers compensation claims handling staff.

Caseloads of the officers appear in parentheses below each position title. The officers' indemnity caseloads average 161, which is below our recommended maximum of 175. Still, one officer has a caseload of 190, which is excessive and should be monitored monthly. Normally, we would recommend that the County add a claims officer if this caseload remained this high for six consecutive months. However, the caseloads for two other officers (four and seven claims, respectively) are minimal. The Safety and Claims Manager indicated that the caseloads for claims officers will level off as these two individuals become more experienced.

- We recommend that the County monitor this situation monthly. A target date of 10/1/99 should be established to ensure that all claims officers are maintaining indemnity caseloads below 175.

Medical only cases — those claims where the employee has lost no time from work and has no permanent disability — are normally resolved in a very short period of time. Accordingly, medical only caseloads can be higher than indemnity caseloads. We normally recommend a maximum medical only caseload of 350. Most of the claims officers also handle a medical only caseload. None of those medical only caseloads are excessive.

Exhibit VI-1

KING COUNTY
Organization Chart
Workers Compensation Claims Handling Staff

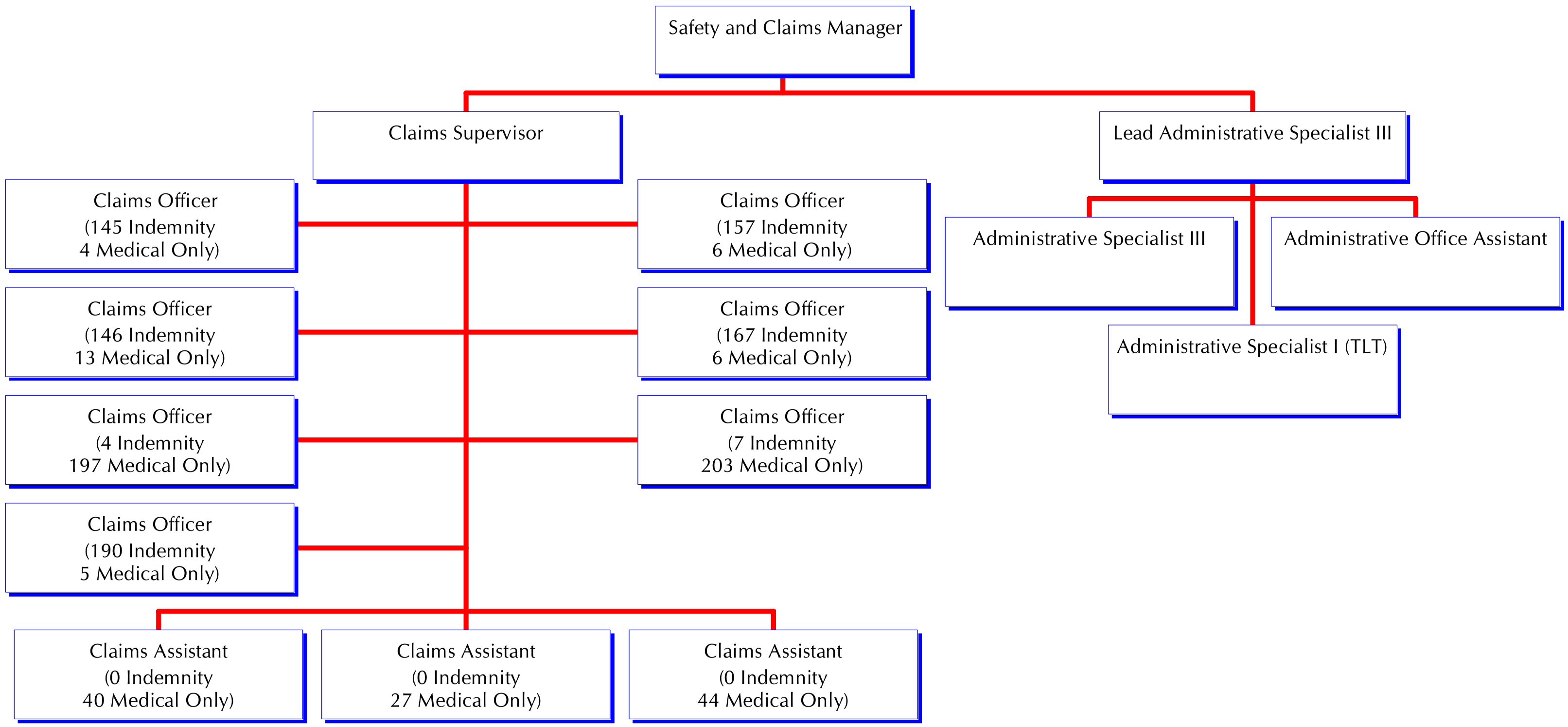


Exhibit VI-1 on page 46 indicates that some officers have higher medical only caseloads than others. The medical only caseload is usually an indication of the individual's indemnity claims handling experience. In other words, those officers with more experience handling Washington indemnity claims have smaller medical only caseloads. This is appropriate.

- Based on reviews of resumes and discussions with claims handling personnel, we conclude all personnel are qualified to handle Washington workers compensation claims.

b. Claims Reporting Process

The reporting process discussed here pertains to the process implemented after the County assumed the handling of Metro claims (approximately three years ago). Currently, Metro employees report losses to their direct supervisor. The supervisor provides the employee with an information packet. It is the employee's responsibility to complete the SIF-2 (Employer's First Report of Industrial Injury).

Our review of files can identify no trend in late reporting. A couple of claims appear to have been received late by the Workers Compensation Unit, but no negative fiscal impact can be identified as a result of this late receipt.

The Safety and Claims Manager indicated it is her goal to implement a process whereby injured employees can contact their designated officer (claims handler). The Workers Compensation Unit's goal to assign cases of particular County divisions to specific claims officers will accomplish this. Currently, claims officers handle claims by alphabetical last name of the injured employee.

- As an additional claims management tool, we recommend the County develop an initial claim evaluation checklist to be completed by the claims supervisor prior to distributing the assignment to the officer. That initial checklist should contain, at a minimum, the following instructional categories:

  — Recommended initial reserves.

  — Recommended plan of action (e.g., no contact in instances where a formal claim has not been presented).

— Plan of action (e.g., investigation to be undertaken).

— Other issues, such as identification of coverage questions or need to incorporate the opinion of the Prosecuting Attorney Office.

c. Investigation

To comply with accepted industry standards, the following investigative activity must occur:

- Contact with the injured employee within 24 hours of the officer's receipt of loss notice.
- Identification and contact of witnesses.
- Verification the injury is work related.
- Research or indexing of injury history to identify past similar injuries which may have contributed to the employee's current injury.
- Obtain recorded or written statements regarding the incident from injured employees or witnesses.
- Follow-up contact with medical providers to gain a clear understanding of injury severity and anticipated duration of disability.
- Obtain police accident reports when the industrial injury is the result of an incident reportable to the police (e.g., auto accident).
- Obtain updated wage information to accurately calculate temporary total disability (TTD) benefits.

1) ***Contact.*** Initial contact of the employee should be made within 24 hours of the claims handler's receipt of loss. If verbal contact cannot be established within seven working days, a letter should be sent to the claimant requesting return contact.

   The files exhibit minimal compliance with this standard. We realize there is no written procedure in place for initial contact. Our comments here are to provide a recommendation to the County for industry standard compliance.

- We recommend that the 24-hour standard regarding employee contact should be a clear written procedure in any claims procedures manual developed by the County.

2) ***Compensability Determination.*** The files reflect detailed documentation confirming the County's compensability decision. Additionally, the determination of the involved employee's conjugal situation was clearly documented. The maximum weekly temporary disability rate paid to injured Washington employees is based on a percentage of that individual's wages. The percentage can be between 60% - 75% of the employee's average weekly wage. The percent used is influenced by the employee's conjugal situation. Conjugal refers to such matters as:

   — Whether the employee is a provider for dependents.

   — The employee's marital status.

   If either of these two factors are relevant to the involved employee, the percentage of the employee's wage to be compensated for by workers compensation temporary disability benefits increases.

3) ***Indexing.*** The County subscribes to The Index System, a nationwide database of injury history. However, indexing of injured employees has only been performed consistently in roughly the past year. We encourage the County to continue to index all injured employees presenting lost time claims.

4) ***Recorded/Written Statements.*** It is not always necessary to obtain permanent records of the claimants' and witnesses' recollection of the incident. Workers compensation providers are statutorily obligated to provide benefits for compensable claims. However, disputed claims (denied or delayed) may require statements of witnesses (e.g., co-workers) and the injured employee to support compensability decisions.

   Most recorded statements are conducted by the handling officer, although the County may utilize outside firms if the statement must be taken in remote areas of the State. The files reflect appropriate activity in this area of claims handling.

5) ***Follow-Up Contact with Medical Providers.*** The files exhibit aggressive attempts to conduct follow-up pursuit of medical

providers. Continued communication with the provider ensures that any indication of maximum medical improvement (MMI) status will be identified quickly, thus, resolving the claim without unnecessary benefit expenditure. MMI refers to the point at which the employee's injury has reached the maximum impact to that employee's ability to assume his or her usual and customary job duties. Essentially, the employee's disability will get no worse. This designation normally requires the confirmation of a treating physician. It is at this point that the employee's permanent disability can be calculated since no further/additional disability is anticipated.

6) ***Wage Information.*** Wage information must be obtained to verify the average weekly wage of injured employees. Calculation of the average weekly wage dictates whether the employee will receive the maximum TTD benefit.

Claims handlers are obtaining wage information consistently.

d. Subrogation

Seven files reviewed involve subrogation issues. Those files lack aggressive subrogation pursuit. Table IV-1 below discusses the 7 subrogation claims.

Table VI-1
King County
Subrogation Analysis (Workers Compensation)

Claim No.	Comments
W304703	The employee fractured his thumb and middle finger in an altercation with a suspect. The file contains a letter from the County to the employee advising of its lien rights. However, no follow-up communication appears in the file. Also, no documentation appears on the subrogation screen of the County's risk management information system (RMIS).
W304456	The employee (a Metro bus driver) was assaulted by a passenger. No subrogation pursuit is exhibited in the file, although a 10/15/98 note indicates the officer was attempting to obtain a police report in order to identify the responsible party.
W198313	The employee sustained a serious brain injury when a tire exploded. The file contains no mention of subrogation. Some attempt to identify the manufacturer of the tire or any tools that may have caused this accident should have been made.

Claim No.	Comments
W198296	The claimant was hit in the head by a pipe during an inspection. The file contains a letter to the employee advising of the County's lien rights. This letter is dated 11/6/97. The file contains no follow-up subrogation activity.
W303779	This is a slip and fall accident which, probably, has minimal subrogation potential. Still, the letter to the employee advising of lien rights was issued on 2/25/99. The claims officer received notice of this loss on 12/30/98. The lien letter was sent nearly two months after receipt of loss. Initial notices of subrogation activity should be issued within 14 days of the claims handler's receipt of loss notice.
T404899	The employee fractured her finger when it was caught in a hoist. This file appears to have some subrogation potential (i.e., the manufacturer of the hoist). No comments pertaining to subrogation appear in the claim file.
W196986	The claimant strained her back in an automobile accident. A letter was issued to the employee dated 9/11/97 advising of the County's lien rights. The file contains no subsequent follow-up documentation.

The failure to pursue responsible parties for the recovery of disability benefits paid by the County can result in a substantial loss of recoverable funds.

- We recommend that the County aggressively pursue subrogation opportunities whenever it is appropriate to do so.

e. Litigation Management

When evaluating this category, we sought to verify that:

- Officers are promptly recognizing litigation issues.
- Cases are referred to defense counsel in a timely manner.
- Claims handlers are reviewing defense counsel bills and confirming reasonableness of those bills.
- Claim files document some plan for litigation activity.

Only 7 of the claims involved some element of litigation.

Claims officers are effectively managing litigation on County workers compensation claims. Defense counsel is provided by the Prosecuting Attorney Office. All litigated files contain active communication between defense counsel and the officer.

2. Fiscal Categories

We evaluated the County's compliance with accepted industry standards in the following fiscal categories:

- Calculation/Accuracy of reserves.
- Timeliness and accuracy of TTD payments.
- Timeliness and accuracy of permanent disability (PD) payments.
- Appropriate application of vocational rehabilitation services.
- Timeliness of medical payments.
- Effective use of cost containment measures.
- Appropriateness of claim closure/settlement.

a. Reserving

County claim reserves should anticipate the most probable case value and be based on:

- Information contained in the SIF-2 Form
  (Employer's First Report of Occupational Injury or Illness).
- Information contained in any reports submitted by treating physicians.
- Anticipated TTD benefits.
- Anticipated loss of earning power (LEP) benefits.
- Anticipated medical costs.
- The employee's wage information.
- Anticipated vocational rehabilitation (VR) benefits.
- Anticipated PD benefits.

Claims handlers are generally considering these and other factors when establishing and amending claim reserves. Only 6 of the 89 open claims reviewed (75 indemnity; 14 medical only) require a reserve change. Exhibit VI-2 on page 54 discusses those claims.

A previous section of this chapter commented on our recommendation that an initial claims handling instructional checklist be completed by the supervisor. One of the key components of that checklist would be the supervisor's initial reserve instructions.

b. TTD Benefits

We reviewed TTD payments to determine timeliness and accuracy. We verified that TTD is calculated correctly based on the employee's average weekly wage and that the payment is issued within 14 days of the first date of disability.

Other factors considered to ensure the accuracy of TTD benefits are:

- Consideration of King County's Kept On Salary (KOS) policy. This consideration does not apply to Metro employees. KOS serves, essentially, as a salary continuation plan for County employees. This ensures injured employees that they will receive their normal wage even if unable to work due to a work-related injury. The portion of the employee's salary which represents workers compensation benefits is not taxable in this situation.

  If, for example, the employee's average weekly wage is $1,000 and his/her workers compensation temporary disability rate is $600, the KOS policy would ensure that the employee receives the additional $400. He/she would only be taxed on the $400 KOS disbursement.

- Consideration of the salary continuation policy provided for Metro employees. This salary continuation program is part of the current contract the County has with ATU Local 587. Essentially, the salary continuation provisions are:

  — For the first 3 months of unemployment, the employee receives 100% of his/her net pay.

  — From 3 to 6 months, the employee receives 90% of his/her net pay.

  — From 6 to 9 months, the employee receives 80% of his/her net pay.

Exhibit VI-2

KING COUNTY
Workers Compensation Reserve Analysis

Claim No.	Current Outstanding Reserve	Recommended Outstanding Reserve	Comments
W304630	$0 (Vocational rehabilitation)	$5,000 (Vocational rehabilitation)	The file documents a vocational rehabilitation issue. It is unclear why no reserve has been established for this exposure.
W304030	$3,335 (Medical)	$7,500 (Medical)	It appears a second surgery may be required.
W304703	$508 (Indemnity)	$2,500 (Indemnity)	A report from a treating physician indicates a potential permanent disability award of 3%. The current indemnity reserve seems inadequate.
T900852	$3,732 (Vocational rehabilitation)	$0 (Vocational rehabilitation)	The Washington Department of Labor and Industries (DLI) issued a notice indicating the claimant was "not eligible" for vocational rehabilitation benefits. This notice was issued on 12/4/97.
T858300	$5,379 (Vocational rehabilitation)	$0 (Vocational rehabilitation)	Similar to the previously mentioned claim, a notice from the DLI indicating ineligibility was received by the County on 7/9/98.
W116090	$0 (Indemnity)	$3,000 (Indemnity)	The employee's attorney is demanding three months' lost time benefits. This benefit was denied on 12/18/98, but the attorney is persisting in his demand for these benefits. As a precaution, an indemnity reserve should be established.

These salary continuation benefits are provided from a separate Transit fund.

We conclude that the separate salary continuation plans are equitable.

- Consideration of Washington's policy allowing for "provisional" payments even while the claim is in delay status.
- Consideration of conjugal situations — permissible in Washington.

Generally, claims handlers are considering these factors when calculating TTD benefits. We identified only 2 instances where TTD seemed to have been calculated incorrectly. Those claims are discussed in Table VI-2 below.

Table VI-2
King County
TTD Benefit Calculation Analysis

Claim No.	Comments
W392314	Claims handlers routinely provided a daily rate calculation. In this instance, the file reflects a daily rate calculation of $35.87 per day. Wage information provided in the file resulted in our wage calculation of $54.62 per day.
W303806	The file lacks clear documentation as to how the monthly TTD rate was calculated. The current monthly wage is $3,653.60. Our calculation results in a TTD monthly benefit rate of $2,192.16. The County has calculated a monthly TTD rate of $2,520.98.

It is possible that conjugal influences were not documented clearly. Our calculations relied solely on material contained in the claim file.

c. Timeliness of Medical Payments

Accepted industry standards require that all medical billings be matched to the file, reviewed for correctness, approved for payment and paid within 30 days of receipt. Medical bills deemed unrelated to the injury should be objected to within this 30-day period.

Claims handlers are complying with this standard on indemnity and medical only files.

d. Cost Containment

Thorough scrutiny of all medical bills to identify charges not in compliance with Washington's fee schedule and charges or treatments that are not work related is vital. A complacent cost containment policy can result in thousands of dollars in unnecessary payments on a single claim.

Tools available to a workers compensation provider that can mitigate costs are:

- An effective and aggressive light duty/return-to-work program.
- Logical and effective use of case management services.
- Use of a bill review service to ensure fee schedule compliance.

Cost containment on County claims are performed by the following vendors:

- Case management/utilization review — Medical Audit Consultants (MAC).

- Medical bill review — done automatically on the County's RMIS. *Most claims RMIS have on-line medical bill review capabilities. States which have developed a medical fee schedule assign a maximum possible fee for particular treatments. Most RMIS simply incorporate this maximum allowable charge for the code which corresponds to the particular treatment. When the particular code is input to the RMIS, the RMIS will ensure that any fee for that treatment is at or below this maximum fee.*

  This RMIS capability actually saves the County funds because an outside medical bill review firm is not required to ensure fee schedule compliance.

The County is practicing effective cost containment. For example, its fee schedule compliance efforts resulted in savings on medical bills of $1,405,016, or 27% of the original amount billed. For calendar year 1998, this savings is similar to savings experienced by other entities we are familiar with.

The fee schedule compliance savings number was obtained from the Safety and Claims Manager and represents savings on all medical bills processed for calendar year 1998.

e. Claim Closure/Diary

The decision to accept or deny a claim should be made within 90 days of knowledge of the claim. Failure to decide the compensability within 90 days may raise a rebuttal presumption that the injury is work related.

We normally recommend an active indemnity file be reviewed by the handling officer every 30 days, at minimum. Any activity conducted on the date of claims officer review must be documented in the file. Generally, County claims officers are effectively documenting activity. This activity is occurring in timely intervals. Our only concern pertains to the medical only files. Of the 14 files reviewed, 4 (31%) lack timely activity. Those 4 claims are discussed in Table VI-3 below.

Table VI-3
King County
Claim Closure/Diary Analysis

Claim No.	Comments
W392265	A standard $250 medical reserve was established on this claim, generated when the employee was exposed to chemicals. The last activity documented in the file was 12/29/98.
W392466	A standard $500 medical reserve was established on this file. There was no activity between the dates of 12/4/98 - 2/26/99 (the day of our review).
W116575	A 20-day letter advising the employee that the claim would be closed without future activity was issued on 12/11/98. As of the date of our review (2/26/99), the file was still open despite no subsequent documentation received from the employee.
W197361	The last treatment documented in this file is March 1998. The last activity documented is May 1998. A 20-day letter advising the employee of the County's intent to close the file was issued on 4/16/98. The file was still open on the day of our review.

3. Claims Management Categories

a. Supervision

The workers compensation claims handling unit is in transition. Specifically, the Safety and Claims Manager assumed her management position less than six months ago and a supervisory position was vacant at the time of our review. Still, we can identify no negative claims handling directly attributable to the lack of a claims supervisor. Also, we were advised that the claims supervisor position had been filled and that individual started with the County on 3/1/99. We completed our review of the workers compensation program on 2/26/99. Accordingly, we are unable to assess the current supervisory situation.

We reiterate our comments in the reserve section of our workers compensation analysis which state that supervisory review of initial case reserves is a routine and vital function of an efficiently run workers compensation program.

b. Creation of Claims Handling Procedural Document

Currently, there is no detailed claims handling procedural document utilized by the County.

- We strongly recommend that the County develop a claims handling procedural manual.

Its advantages are:

- To shield the County from any claims of bad faith/incompetent claims handling. The document will provide specific procedures for all elements of claims handling. Assuming the instructions in the document are followed consistently by all claims handlers, no assertion of inconsistent claims handling, and, thus, bad faith can be reasonably asserted.

- To ensure that any new claims handling personnel can quickly assume an active caseload. The document should be used as a reference to instruct new employees on the claims handling policies of the County thus mitigating the time necessary to fully train new employees.

B. METRO LIABILITY CLAIMS MANAGEMENT ANALYSIS

Our claims handling comments and recommendations focused primarily on activity exhibited by Crawford. The bulk of our fieldwork pertaining to Metro liability claims management analysis was performed at Crawford's servicing office. However, we considered the following unique claims handling arrangements when evaluating overall claims handling performance on Metro liability claims:

- Crawford's handling of Metro claims is limited, in that cases which develop potential litigation are referred back to the Prosecuting Attorney Office and the County Risk Management Office.

- Approximately 20% of claims assigned to Crawford are referred (subcontracted) to Classic Claims Service (CCS) in Everett.

- Ongoing investigation and claims handling of Metro claims after the cases are referred back to the Prosecuting Attorney Office may also be handled by Tort Investigators within the Prosecuting Attorney Office.

1. Staffing/Caseloads

County Metro liability claims are handled by various Crawford personnel. Exhibit VI-3 on page 60 displays the organizational structure of Crawford claims handling personnel assigned to the County. Caseloads appear in parentheses below each position title.

We normally recommend a maximum caseload of 150 for an adjustor assigned to the type of liability claim typical for Metro-type exposures (e.g., transit operations). Routinely, these liability claims involve a higher percentage of litigation.

We also sought to assess the degree of experience of individuals assigned to Metro claims. All Crawford individuals listed in Exhibit IV-C have the requisite experience to handle transit/waste water claims. We point out that we did not meet with CCS. Any observations of CCS' performance were obtained randomly through the review of Crawford claim files. Again, our primary focus here is on Crawford's performance and the reasonableness of its involvement on Metro claims. However, as a contract vendor utilizing a subcontractor, Crawford is ultimately responsible for performance and would, most likely, indemnify the County if CCS' work product was the sole cause of some negative fiscal impact to the County.

2. Timeliness/Efficiency of Claims Loss Reporting

Similar to other transit exposures we are familiar with, Metro claims are generated primarily by bus/coach operations. Also, roughly half of all incidents do not get reported to the involved driver. Based on discussions with Crawford and County personnel, we understand the following chronology of reporting exists:

- If an incident is reported to the driver, the driver gives a card to the claimant which is used to provide the driver with relevant information on the claim.

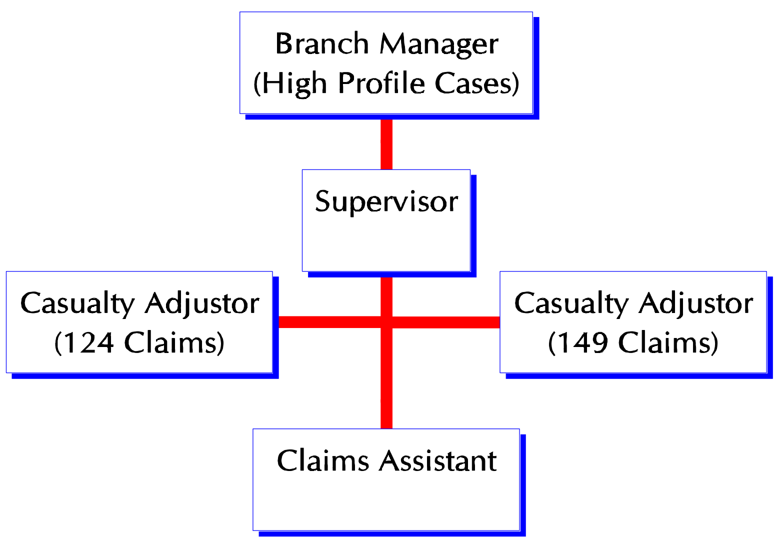
- The driver will complete a report of the incident.

- Crawford receives these driver reports daily and returns reports which indicate no injury or no damage back to the County for handling.

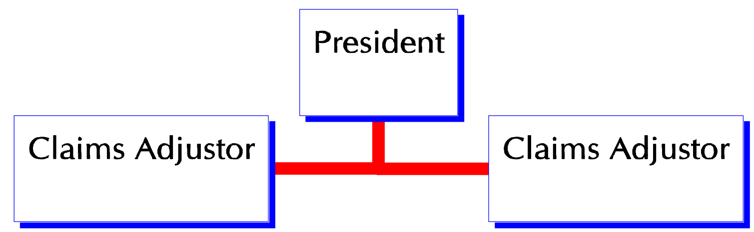
Exhibit VI-3

KING COUNTY
Organizational Chart
Metro Liability Claims Handling
(Contracted Service)

CRAWFORD & CO.



CLASSIC CLAIMS SERVICE



Since our visit to Crawford, the Supervisor has been reassigned. Crawford now is pursuing a "Team" approach to managing the King County account. The Branch Manager still manages the account, but responsibility for day-to-day adjusting activity is now assigned to a Casualty Adjustor.

- If a formal claim is presented, the claim is assigned to a Crawford adjustor. If no formal claim is generated from the incident, the claim is deemed an incident only.

Metro's reporting process is typical for other transit agencies we are familiar with. We make no recommendation for amending this policy.

3. Reserving Accuracy

Metro liability claim reserves should be based on:

- Anticipated extent of damages/injuries sustained.
- Degree of liability attributable to the County, based on a consideration of Washington tort law.
- Existence of additional tortfeasors (responsible parties who may share culpability).
- Application of statutory defenses or immunities available to the County.
- History of settlement trends in the loss venue.
- Anticipated cost of defense, if applicable.

Crawford establishes initial and amended reserves, but must advise the County Risk Manager if total incurred reserves on any particular claim exceed $25,000. Reserves are reviewed every 60 days. These reserving guidelines are appropriate. We make no recommendation for altering the current procedure.

None of the Crawford claims reviewed require reserve adjustment. We concur with the established reserves on all 71 claims.

Our reserve analysis reflects our opinion only. Our observations are based on experience auditing other Washington public entities and other transit operations.

4. Settlements/Negotiations

Our comments here pertain not only to the Crawford claims handling policies but also the settlement/negotiation process exhibited in the corresponding Prosecuting Attorney Office file. We reviewed 8 Prosecuting Attorney Office files which corresponded to 8 Crawford files. This enabled us to follow the settlement/negotiation process from start to final resolution.

Claim settlement authority levels are:

- $0 - $5,000 — Crawford
- $5,001 - $50,000 — County Risk Manager
- $50,001 and above — County Executive

We are advised that any settlement of $2,500 or more requires the ***review*** of the Prosecuting Attorney Office. We do not interpret this as an authority requirement guideline. In other words, it is our understanding that Crawford would not need to refer a $2,700 property damage settlement to the Prosecuting Attorney Office for approval.

These authority levels are reasonable and similar to other public agencies/transit agencies we are familiar with. We make no recommendations for changing the authority levels.

One of the 8 Metro files reviewed at Crawford, which were cross referenced when we reviewed files at the Prosecuting Attorney Office, seems to have been settled for a higher amount than we see with similar entities in the Western United States. Prior to discussing that claim, we feel it is important to acknowledge the following:

- Based on discussions with Prosecuting Attorney Office personnel, we are aware of the adversarial arbitration system in Washington. The County's experience in arbitration reveals that the arbitrators are routinely pro-claimant. Accordingly, the County's success in receiving defense verdicts or mitigated settlements are often limited.

- We do not purport to be legal experts and make no comments pertaining to the legal competence of Prosecuting Attorney personnel. In fact, while sounding subjective, we believe the legal activity on the claim discussed below exhibits aggressive efforts to mitigate the County's exposure. Our only concern pertains to the amount of ultimate settlement that follows this aggressive effort.

The claim discussed below is a claim we believe was settled for an amount higher than that supported by the investigation material in either the Crawford or the Prosecuting Attorney Office file:

- ***Claim No. 92207.*** This involves an 81-year-old claimant who was injured when he tripped and fell on a Metro bus. The claimant incurred $2,345 in medical bills for treatment of primarily subjective/soft tissue injuries. We do not suggest the injuries did not exist, but subjective/soft tissue injuries rarely result in permanent disability. This claim was settled for $25,000 on 8/17/98.

Other similar entities we have evaluated settled similar claims for $8,000 - $12,000. This claim was settled prior to an arbitrator's decision. Again, we acknowledge that the arbitration environment in the Seattle/King County area is not favorable to the County, but this settlement seems excessive.

5. Investigation

The establishment and maintenance of accurate reserves on any claim file is, to some extent, dependent on the information gained through the detailed investigation of the circumstances surrounding the claim. For liability claims, a detailed investigation includes:

- Making prompt contact with the injured claimant.
- Verifying the extent of the County's liability through medical reports or property damage estimates.
- Accounting for injury history to determine any pre-existing condition.
- Canvassing for possible witnesses to the incident.
- Obtaining recorded or written statements regarding the incident from the claimant and witnesses, when possible.
- Obtaining police accident reports when the damage or injury was the result of a reportable incident.
- Obtaining photographs of accident scenes and instruments causing the injury, when applicable.
- Aggressive pursuit of additional responsible parties to offset the County's contribution to damage/injury awards.
- Application of indemnification/hold harmless language contained in various contracts the County enters into with vendors.
- Obtaining signed releases/dismissals in cases that have been resolved through legal proceedings or settlement negotiations.

- Consideration of Washington's common carrier statute.

a. **Timely Contact.** Accepted claims handling standards require contact of all claimants within 24 hours of receipt of loss notice. If the claimant is represented, acknowledgment to the claimant's attorney should be provided within five working days of the receipt of loss notice. Crawford is complying with this accepted industry standard.

b. **Verification of Support for Settlement.** In those instances where a bodily injury settlement was effected, the Crawford files, generally, lack the supporting documentation. This material was routinely located in the Prosecuting Attorney Office file. Property damage settlements were consistently supported by estimates or Crawford's own property damage appraisals.

c. **Obtaining Releases.** All Crawford files reviewed were closed files. Accordingly, the majority of these files include the obtaining of releases and/or dismissals. Generally, the Crawford files contained the appropriate releases (usually these are simple property damage releases). However, due to the County's policy of referring bodily injury settlement situations back to the Prosecuting Attorney Office or the Risk Management Office, Crawford files did not contain dismissals/releases. The files listed in Table VI-4 below are examples of those claims lacking a release and/or dismissal.

Table VI-4
King County
Releases/Dismissals Documentation Analysis

Claim No.	Comments
97657	This is a simple property damage claim resulting in a $38 settlement payment. There is no signed release in the file.
92207	This is a bodily injury claim which was ultimately settled by the Prosecuting Attorney Office. The Crawford file does not contain a copy of the signed release.
82818	The claimant tripped and fell on a Metro bus. The claim was settled by the Prosecuting Attorney Office. The Crawford file contains no copy of the release.

Crawford is consistently documenting property damage releases in its files, but we recommend the County begin providing Crawford with a copy of releases/dismissals in those instances where the case was settled by the Prosecuting Attorney Office or the Risk Management Office. This is done for documentation purposes only.

Crawford, as a representative of the County, may be subpoenaed to provide relevant documentation in a case on which it has conducted preliminary investigation. Crawford's ability to fully document final case resolution will not only ensure finalization of Crawford's records, but will also ensure the County that any subcontractor or indemnitor completely document all case activity.

6. Litigation Management

Our comments for this category are limited due to the County's policy of referring all litigated matters to the Prosecuting Attorney Office.

7. File Organization

For this category, we sought to determine that:

- Crawford claim files are organized and in chronological order.
- Material is secured to the file jacket to prevent misplacement.
- Daily adjustor and supervisor documentation is clear and consistent in the note screen of Crawford's RMIS.

Crawford files are consistently in good order. All documentation criteria previously listed is, generally, adhered to. We noted only one exception where some material pertaining to a different claim inadvertently was placed in another file.

8. Risk Management Information System (RMIS)

Crawford uses its own RMIS. We are familiar with this system and believe it is a beneficial claims management tool. Other advantageous characteristics of Crawford's RMIS are:

- CCS has access to this system. This ensures Crawford that all CCS activity will be permanently documented.

- The County Risk Claims Coordinator is responsible for check register reconciliation and has access to the Crawford notes to assist her in this function.

- Crawford indicates that their system is Y2K compliant. We were not involved in any demonstration of Y2K compliance. Frankly, our theory is that full Y2K compliance cannot be assured until the actual date (1/1/00). Our point here is that Crawford is aware of the importance of Y2K compliance and has attempted to resolve the potential problem well in advance of the compliance date.

9. <u>File Closure</u>

Again, all Crawford files reviewed were closed at the time of our review. We conclude Crawford is aggressively attempting to close files as quickly and reasonably as possible. Many of the files reviewed were referred to the Prosecuting Attorney Office prior to case closure. In those instances, we analyzed Crawford's attempt to provide as detailed investigation as possible to assist the Prosecuting Attorney Office in case resolution. Crawford is accomplishing this and meeting or exceeding industry standards in this area.

10. <u>In-House *Option*</u>

This report section is a cost analysis of the *option* to develop and staff a claims handling unit for Metro claims within the Risk Management Division. We present the cost for the County to hire its own claims handlers, supervisory and support staff to assume the handling of Metro claims. Exhibit IV-4 on page 67 displays the budgetary impact of assuming the handling of Metro claims. Most of the cost data used in Exhibit VI-4 was provided to us by the County.

Exhibit VI-4

KING COUNTY
Metro Claims Handling Cost Analysis

All Amounts are Annualized

Position (1)	Salary [1] (2)	Benefit Load (2) × .32 (3)	Total Cost (2) + (3) (4)	Space Cost (5) [2]	Total Annual Cost (4) + (5) (6)	One-Time Equipment Cost (7)[3]
Claims Supervisor	$60,000	$19,200	$79,200	$2,947	$82,147	$9,000
Claims Officer — Senior	46,000	14,720	60,720	2,947	63,667	9,000
Claims Officer — Senior	46,000	14,720	60,720	2,947	63,667	9,000
Claims Clerk	30,000	9,600	39,600	2,947	42,547	9,000
Receptionist	23,000	7,360	30,360	2,947	33,307	9,000
Total Personnel Costs	$205,000	$65,600	$270,600	$14,735	$285,335	$45,000
Outside Investigation					25,000	
Training Costs (e.g., attendance at seminars; pursuit of related additional education)					25,000	
Total Annual Cost					$335,335	

Notes:

1 Salaries provided by County Risk Management Office. However, we augmented these salaries by approximately 20% due to an extremely tight job market in Seattle and our awareness of current salaries for experienced liability technicians in the area.

2 Based on space availability analysis performed by County Risk Management Office.

3 One-time equipment cost includes roughly $7,500 for computer terminals and associated systems costs and approximately $1,500 for furniture and various other office necessities ($9,000 per individual).

We arrived at these figures by considering the following information:

- The County incurs approximately 1,650 new automobile liability claims each year; 50 new general liability claims each year; approximately 1,700 incident-only reports each year.

- At the time of our review of claims at Crawford, there were approximately 295 open claims.

- Our staffing recommendations consider a maximum liability caseload of 150 open claims. All technical claims handlers should be experienced in the handling of both automobile liability and general liability claims. Automobile liability and general liability claims are relatively similar in extent of investigation necessary. Accordingly, the maximum caseload recommendation is similar for both types of losses.

- Nearly all investigation pertaining to these claims will be done by the County claims staff. Still, we recommend the County budget an additional $25,000 per year for outside investigation work necessary in remote parts of the State.

The decision to assume the handling of Metro claims involves more than monetary factors. Other items the County should consider are:

- **Relationship with Prosecuting Attorney Office.** Our review of Crawford files revealed an excellent working relationship with the Prosecuting Attorney Office. However, we are aware that Crawford's handling often is concluded prior to complete investigation. In these instances, the Prosecuting Attorney Office assumes handling and investigation of the file. Still, communication between Crawford and the Prosecuting Attorney Office is effective.

  The use of County employees to handle Metro claims near the Risk Management Office in downtown Seattle will, in our opinion, maintain the effective communication between claims handling personnel and Prosecuting Attorney Office personnel.

- **Management Control.** Even though the County maintains extensive control over Crawford's handling of County claims, the County is not in complete control over staffing. There has been staff turnover at Crawford. This is somewhat endemic in the independent claims handling industry. While there is no guarantee that turnover will not exist if the claims handler is a County employee, we suspect that County employees will have more longevity, primarily due to the increased benefits available to public employees. Also, the County will have complete control over the staffing for the Metro claims handling unit.

Finally, any changes to claims handling policy can be immediately implemented and will not require the input of the outside claims administrator.

- **Cost Comparison.** Our cost analysis calculates the total annual cost to assume the handling of Metro claims is $385,335 in the first year. The County currently pays Crawford $44,632 per month for claims administration services. This equates to an annual cost of $535,584. Accordingly, the County could save $150,249 in the first year and even more in additional years if it assumes the handling of Metro claims.

In-House Conclusion/Recommendation

- Due primarily to the expected cost savings resulting from the internalization of Metro claims handling, we recommend the County consider assuming this responsibility.

If the decision is made to form an internal Metro claims handling unit, the County should anticipate six months before full assumption of Metro claims handling responsibilities is achieved. During that six-month period, we recommend the County consider the following chronology:

- Advertisement of positions available in local publications and newspapers. The County may also want to place advertisements in risk management/claims publications such as *Public Risk* and *Business Insurance*.

- The first individual hired should be the Claims Supervisor. This individual can work with the County Risk Management Office to finalize procedures and to assist in the hiring of the remaining staff.

- Claims technicians (officers) should be hired. We recommend the County anticipate up to two months to advertise for these positions, conduct interviews and select the officers.

- All positions should be filled within one month of full assumption of claims handling responsibilities. Once all positions are filled (fifth month), the County should assume the handling of ***new*** losses.

- After six months, the County should assume the handling of all remaining claims handled by Crawford.

C. NON-METRO LIABILITY CLAIMS MANAGEMENT ANALYSIS

For this element of our report, we focused primarily on the claims handling policies of the County's internal claims management staff. However, the Prosecuting Attorney Office involvement is slightly more extensive than other large County governments we are familiar with. Accordingly, we devoted significant additional time interviewing Prosecuting Attorney Office personnel and reviewing their work product. Examples of Prosecuting Attorney Office involvement, which differs slightly from other similar County governments, are:

- The Prosecuting Attorney Office must review all settlements greater than $2,500.

- The Prosecuting Attorney Office may recommend loss reserves.

  It is not unusual for the legal arm of a county government to recommend legal expense reserves, but King County's Prosecuting Attorney Office may provide loss reserve recommendations as well.

  We make no recommendation for changing the County's policy of loss reserve input by the Prosecuting Attorney Office, so long as that reserve input is advisory only. Ultimately, the decision on the proper loss reserve should be made by a claims professional. The input of the Prosecuting Attorney Office is valuable, but should not be unilateral.

1. Staffing/Caseloads

Exhibit VI-5 on page 71 displays the organizational structure of the claims handling personnel in the County Risk Management Office. Caseloads appear in parenthesis below each position title. The organizational structure of the Tort Section at the Prosecuting Attorney Office appears in Exhibit VI-6 on page 72.

Exhibit VI-5

KING COUNTY
Organizational Chart
Non-Metro Claims Handling Staff — Risk Management Office

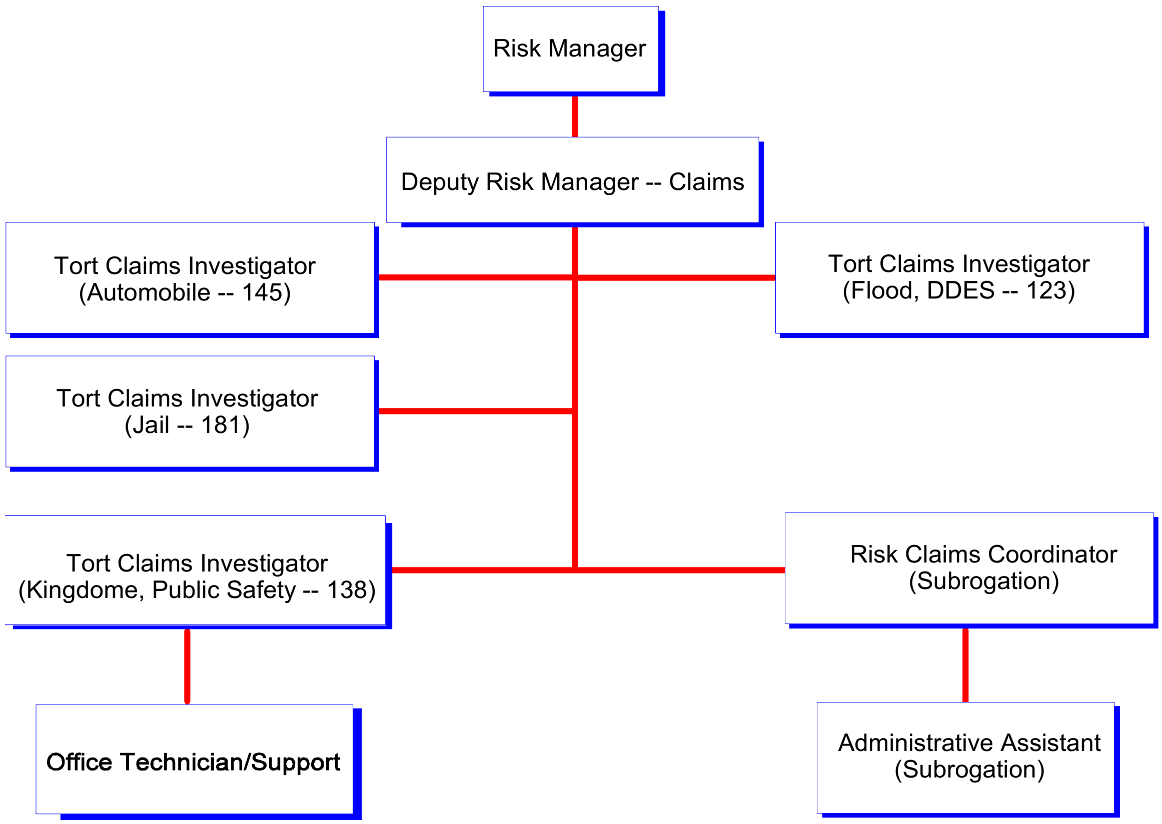
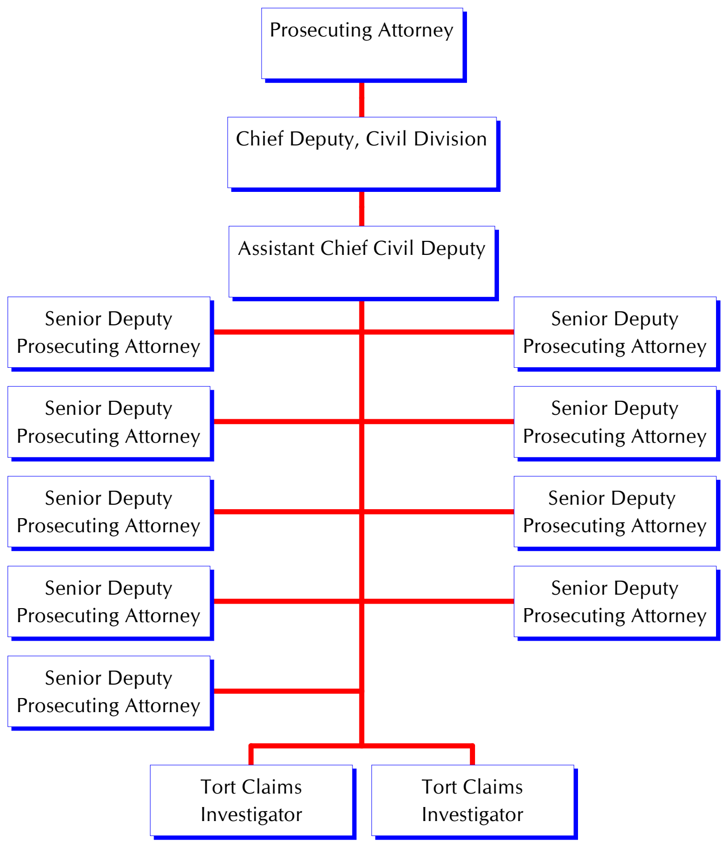


Exhibit VI-6

KING COUNTY
Organizational Chart
King County Prosecuting Attorney Office — Tort Section



Similar to our caseload recommendations for Metro claims, we normally recommend a maximum caseload of no more than 150 active files per adjustor. Only one individual's caseload exceeds our recommended maximum. However, County personnel have advised that an additional officer should be hired sometime in 1999. We encourage the County to monitor the situation closely. Should this individual's caseload remain at its current level for more than six months, some of his assignments should be referred to other officers.

All County claims handling personnel have the requisite experience to handle liability losses normally incurred by county governments such as King County.

2. Timeliness/Efficiency of Claims Loss Reporting

Specific requirements of County personnel are listed in Chapter 4.12.060C of the King County Charter. Requirements set forth in that section of the Charter are similar to requirements we see for other county governments. Likewise, requirements pertaining to the procedures for handling claims (e.g., claim filing requirements, statutory periods within which the claim is deemed actionable and the transmittal requirements of the Clerk of the County Council) are similar to other county governments we are familiar with.

Our review identified no deficiency in the timeliness within which claims handlers receive first notice of loss.

Once claims are received by the County Risk Management Office, the Deputy Risk Manager assigns the claim to a specific technician. Physical claim files are created by office technicians. These procedures are common. We make no recommendation for changing the claims reporting/set-up procedure.

3. Reserving Accuracy

Non-Metro liability claim reserves should be based primarily on:

- Anticipated extent of damages/injuries sustained.
- Degree of liability attributable to the County, based on a consideration of Washington tort law.
- Existence of additional tortfeasors.
- Application of statutory defenses or immunities available to the County.
- History of settlement trends in the loss venue.
- Anticipated cost of defense, if applicable.

Reserve establishment policies are:

- For smaller claims (e.g., the demand is less than $1,000) the reserve is set at the demand amount. This comprises approximately 50% of all claims received by the County.

- Claims officers establish reserves on larger claims, but those reserves are reviewed by the Risk Manager and the Deputy Risk Manager — Claims every six months. These claim reserve establishment policies are reasonable.

Exhibit VI-7 on page 75 discusses 4 open files which, we conclude, require reserve adjustment. We also point out that it was impossible to determine the accuracy of reserves on the 28 closed files reviewed at the County Risk Management Office. This is not unusual as reserves are routinely zeroed out after closure. We could not determine the accuracy of reserves during the "open" phase of the claim for these 28 claims because we reviewed them after they had been closed.

4. <u>Settlements/Negotiations</u>

We, again, incorporate our evaluation of claims settlement policies exhibited in the Prosecuting Attorney Office files reviewed for non-Metro claims.

Settlement authority guidelines are established in Chapter 4.12.070D of the King County Charter. Those settlement authority levels are the same as those indicated in our discussion of Metro claims. Essentially:

- $0 - $50,000 — County Risk Manager.

- $50,001 and above — County Executive.

- All settlements of $2,500 or more for bodily injury and $5,000 or more for property damage require the notification and advice of the Civil Division of the Prosecuting Attorney Office.

These authority levels are reasonable. We make no recommendations for altering the authority levels. Also, we identified no claims where these authority levels were exceeded.

Exhibit VI-7

KING COUNTY
Non-Metro Liability Claims Reserve Analysis

Claim No.	Current Outstanding Reserve	Recommended Outstanding Reserve	Comments
25546	$5,000 (Loss)	$15,000 (Loss)	The claimant tripped and fell in a drainpipe and fractured her foot. No medical documentation has been received yet and liability is uncertain, but claims of this nature (bone fracture) routinely settle for amounts greater than the current outstanding reserve.
25898	$3,000 (Bodily injury)	$7,500 (Bodily injury)	The claimant's vehicle was struck by a County vehicle. Liability seems likely against the County. The file indicates approximately $1,759 in medical costs has been incurred. The current loss reserve does not seen adequate to cover the potential settlement on this claim.
24265	$3,000 (Bodily injury)	$25,000 (Bodily injury)	The claimant slipped and fell at the Kingdome. The claimant is represented and has, allegedly, incurred nearly $12,000 in medical costs. The file also seems to indicate that the claimant is still being treated for her injury.
25301	$2,000 (Bodily injury)	$15,000 (Bodily injury)	The claimant tripped and fell at the Kingdome and fractured his arm. The claimant is a minor and the injury seems fairly serious, although no medical confirmation has been received yet.

Our discussion of Metro liability claim settlements focused on one claim which we believe was settled for an amount higher than that supported by investigation material. We also questioned the settlement of one non-Metro claim:

- ***Claim No. 24949.*** The claimant was injured when his vehicle was struck by a police vehicle. The claimant's injuries were minor and subjective. His medical expenses and wage loss of $16,523 were incurred in only four months. This is excessive and unusual even considering the surgery performed on the claimant approximately one month after the accident. Material we reviewed did not confirm that the required surgery was directly attributable to this incident.

  The claimant is a landscape architect and some correspondence in the file indicates the claimant's own attorney admits that the injury was, to some degree, pre-existing. The claim was settled for $75,000 on 11/30/98. Other similar entities we are familiar with settle claims of this nature for $40,000 - $50,000.

5. <u>Investigation</u>

The establishment and maintenance of accurate reserves on any claim file is, to some extent, dependent on the information gained through the detailed investigation of the circumstances surrounding the claim. For liability claims, a detailed investigation includes:

- Making prompt contact with the injured claimant.
- Verifying the extent of the County's liability through medical reports or property damage estimates.
- Accounting for injury history to determine any pre-existing condition.
- Canvassing for possible witnesses to the incident.
- Obtaining recorded or written statements regarding the incident from the claimant and witnesses, when possible.
- Obtaining police accident reports when the damage or injury was the result of a reportable incident.
- Obtaining photographs of accident scenes and instruments causing the injury, when applicable.

- Aggressive pursuit of additional responsible parties to offset the County's contribution to damage/injury awards.

- Application of indemnification/hold harmless language contained in various contracts the County enters into with vendors.

- Obtaining signed releases/dismissals in cases that have been resolved through legal proceedings or settlement negotiations.

a. **Timely Contact.** Accepted claims handling standards require contact of all claimants within 24 hours of receipt of loss notice. If the claimant is represented, acknowledgment to the claimant's attorney should be provided within five working days of the receipt of loss notice.

Based on our review of file material, we conclude that County claims handlers are not consistently complying with this industry standard. Seven of the 33 (21%) open files reviewed at the County Risk Management Office exhibit late contact. Those claims are discussed in Table VI-5 below.

Table VI-5
King County
Timely Initial Contact Analysis

Claim No.	Date Received by County	Date First Documented Contact
25785	1/7/99	2/9/99
25898	1/21/99	2/8/99
25826	1/11/99	2/8/99
25424	10/27/98	12/10/98
25427	10/28/98	12/4/98
24923	7/27/98	8/19/98
25301	10/7/98	11/5/98

- We recommend that the County adopt the standard of contacting claimants within 24 hours after notice of loss is received and include it as a written procedure in the claims procedure manual.

b. **Verification of Support for Settlement.** All the files, generally, contain detailed information pertaining to the injury/property damage which generated a settlement payment. The files contain detailed medical documentation and property damage estimates.

c. **Obtaining Releases.** The non-Metro files exhibit consistent release/ dismissal documentation. Additionally, all settlement authority approvals are consistently documented in the claim files.

6. Litigation Management

Again, our evaluation of King County litigation management for non-Metro claims was heavily influenced by Chapter 4.12.050 (Role of Prosecuting Attorney) of the King County Charter. Our review of that legislative language indicates Prosecuting Attorney Office responsibilities are similar to other county legal divisions/departments we are familiar with.

The evaluation of the competence of defense provided by Deputy Prosecuting Attorneys is outside the scope of this project and our expertise. Our comments here pertain only to the efficiency of the process by which County claim files document legal recommendation and other correspondence.

Discussions with the Assistant Chief Civil Deputy — Civil Division, Tort Section revealed the following litigation handling characteristics:

- Claims with potential high exposure are designated as "coming attractions" by the Assistant Chief Civil Deputy of the Tort Section. The Prosecuting Attorney Office will open a file and monitor it closely, even if it is only an incident.

- Assignments are generally made based on area of experience (e.g., any law enforcement claims are assigned to Deputy County Prosecutors with extensive law enforcement experience).

- The County Prosecutor has the authority to designate certain non-Metro claims as "L" type claims. These are deemed the most serious claims. All investigation done on "L" claims is at the direction of the handling Deputy Prosecuting Attorney. That investigation may be performed by either the Tort Investigators at the Prosecuting Attorney Office or the Risk Management Claims Officers. That investigation is normally considered support for potential subsequent litigation and may include the securing of witnesses' names and photographs/diagrams of accident scenes.

- Washington's arbitration environment is more detailed than other arbitration arrangements we are familiar with. For example, any arbitration is similar to a full trial (e.g., discovery is extensive; decisions can be appealed).

a. **Communication with Risk Management.** Based on discussions with Prosecuting Attorney personnel and our review of claim files, we conclude correspondence between the claims handlers and the handling attorney meets or exceeds industry standards. Also, the involvement of the particular County division (referred to as "client" by the Prosecuting Attorney) is extensive.

Any matter subject to review of the County Executive involves a second opinion. The assigned Deputy Prosecuting Attorney will discuss the matter with the Chief Civil Deputy Prosecuting Attorney. The particular involved division manager is also involved in that discussion.

b. **Litigation Peer Review.** The Assistant Chief Civil Deputy assigns every case within the Tort Section. Any case that requires authority or is a candidate for mediation also generates a file review by him. He also reviews case reserves on litigated files every six months.

c. **Litigation Expense Control/Cost Allocation.** The Prosecuting Attorney Office keeps daily time sheets which are provided to the County Risk Manager for division allocation. Our review of claim files concludes that litigation cost management is effective.

7. <u>File Organization</u>

For this category, we sought to determine that:

- Risk Management non-Metro files are organized and in chronological order.

- Material is secured to the file jacket to prevent misplacement.

- Daily adjustor and supervisor documentation is clear and consistent in the claim file.

County Risk Management Office claim files do not exhibit documentation which meets industry standards. Specifically:

- File material is consistently not secured to the file jacket.

- Material is routinely out of chronological order. Accordingly, it was difficult for us to follow the progress of the claims.

Risk Management Office claims handling personnel indicated that they usually do not organize the claim file until the claim file is resolved. This is highly unusual. This deficiency can be easily remedied by two-hole punching the claim file and inserting a bracket. The primary advantage of a neatly documented file is to ensure that any new employee who assumes a caseload will be able to quickly interpret the status of a claim and mitigate any reduction in the speed with which the case is resolved.

- While we can identify no negative fiscal impact resulting from this documentation deficiency, we recommend the County initiate procedures whereby all claim file material is secured to the file jacket and in chronological order.

8. <u>Claims Procedures Manual</u>

During our review of non-Metro claims, the Deputy Risk Manager — Claims provided us with a copy of the "*The King County Risk Management Claim Manual*." Actually, this document is not a claims procedures manual. Rather, it merely houses form letters used for various types of claims.

- We strongly recommend that the County consider the creation of a manual which will instruct claims handling technicians on day-to-day claims handling activity from initial receipt of loss notice to final resolution. Such a manual should provide detailed instruction in the following claims handling areas:
  - Initial set-up/reporting.
  - Establishment/update of case reserves.
  - Investigation procedures.
  - Litigation management procedures.
  - Payment/settlement authority guidelines.
  - Documentation requirements.
  - Use of risk management information system.
  - Diary/closure requirement.

VII. RISK FINANCING

The goal of risk financing is to assure that funds will be available to pay losses when they occur. There are many risk financing techniques, but most fall into two broad categories:

- Self-insurance.
- Insurance.

The risk financing discipline is applied by estimating the amount of losses that will occur and comparing the cost of handling these losses internally (self-insurance) to the cost of insuring with a commercial insurer (insurance). The proper balance of self-insurance and insurance is the combination that produces the lowest cost of risk in the long run.

To make an informed risk financing decision, one must have access to historical loss data to project future incurred losses. If an entity then chooses to self-insure, it must utilize its actuarial projections to properly finance the payment of its liabilities.

In constructing a risk financing program, it is useful to determine the amount of losses an entity can comfortably finance with its own cash resources and borrowing power. The ability to absorb sudden, unexpected losses is called the "risk retention" capacity. This chapter evaluates the County's risk financing practices.

A. SELF-INSURANCE

King County self-insures its liability and workers compensation losses up to $2.5 million per occurrence and $500,000 per occurrence, respectively, in two separate programs. An actuarial firm determines outstanding loss liabilities for each program.

Below is our analysis of the actuarial service fees, the most recent actuarial review, an assessment of the short- and long-term adequacy of loss reserves (including "catastrophic loss" reserves), and our evaluation of the current programs and other policy options for funding the risk management program.

1. Cost of Actuarial Services

We understand the fees to perform the study in 1998 were $16,000 procured through a competitive bid. The fees are reasonable based upon similar assignments we are familiar with.

2. Recent Actuarial Review

The review includes:

a. **Qualifications of the actuary.** The actuarial study was performed under the signature of Mr. Richard J. Fallquist. Mr. Fallquist is a Fellow of the Casualty Actuarial Society (FCAS) and a Member of the American Academy of Actuaries (MAAA). We are familiar with other actuarial studies performed by Mr. Fallquist. In our opinion, he is professionally qualified to perform the study.

b. **Reasonableness of assumptions.** The study relied on a number of key assumptions. The following is our review:

   1) ***Selection of loss development factors.*** For the most part, we believe the selection of loss development factors is valid. In a few isolated instances, we may have selected other factors. However, as stated below, we find the study conclusions reasonable.

   2) ***Selection of trend factors.*** The actuarial assumptions used were reasonable. We do note that Mr. Fallquist used some unusual exposure data in the study. Exposure data refers to a basis from which to determine trends.

      For example, workers compensation indemnity benefits are based upon pre-injury wage. Payroll is almost always used as an exposure base for similar assignments and in the commercial insurance industry. In a few instances, the number of employees is used. The study used number of bus fleet miles for Metro workers compensation. While the actuary's exposure rates are unusual, it's unlikely they materially affect the study outcome. Costs were measured against the balance of County workers compensation man-hours.

   3) ***Interest rate assumptions.*** The actuary did not use interest rates in the study. This method overstates the amount of funds necessary to have on hand today to pay for future losses because it ignores investment income. Allowing for investment income by calculating the net present value of outstanding loss reserves is acceptable under Governmental Accounting Standards Board (GASB) Statement No. 10 standards.

- We recommend that the County direct its actuary to calculate the net present value of outstanding loss reserves.

c. **Reasonableness of methodology.** The study relied upon four actuarial methods to project losses. The methods are paid loss development, incurred loss development, average loss and percent change, and loss per exposure percent change. Each method is described below:

1) ***Paid loss development.*** Paid losses represent the amounts actually paid to claimants. As time goes on, loss payments continue until all claims are closed and there are no remaining payments expected. At this time, the ultimate limited losses for the claim period are known. This common process is called "paid loss development."

   Paid loss development is an extrapolation of actual dollars paid. It does not depend on case reserve estimates. A potential shortcoming of utilizing this method is that only a small fraction of total payments have been made for the most recent claim periods. Extrapolating ultimate limited losses based on small amounts of actual payments may be speculative. A second potential shortcoming is that payment patterns can change over time.

2) ***Incurred loss development.*** Incurred losses are paid losses plus case reserves. In most workers compensation programs, total reported incurred losses underestimate the ultimate losses. Over time, as more information about a body of claims becomes known, they are adjusted either up or down until the claim is closed. Though many individual claims settle for less than what was estimated, the decreases are, generally, more than offset by increases in the cost of other claims for which new information has emerged.

   The net effect is total estimated costs are often revised upward over time. This normal process is called "incurred loss development." Actuaries typically review the development patterns of the recent past to make projections of the expected future loss development and, therefore, estimations of ultimate limited losses.

3) ***Average loss and percent change.*** This method compares the average cost per claim over time to infer an average by fiscal year. The average cost per clam is multiplied by the number of claims to project losses.

4) ***Loss per exposure percent change.*** The losses per exposure use historical loss rate per exposure units (e.g., number of worked hours for workers compensation) to project a rate by fiscal year. The rate is then multiplied by exposure units to project losses.

The paid loss development and incurred loss development methods are the most common methods used by actuaries for similar projects. The actuary used these methods in a reasonable manner.

We do have some issues with the average loss and percent change method and the loss per exposure percent change method as used in the study. These two methods are intended to add predictive value by inferring loss experience for recent fiscal years based on the experience for older years. However, as used in the iterative manner by the actuary, it is overly dependent upon the final projections and adds little value.

- We recommend the County employ the more traditional method, frequency times severity, instead of the average loss and percent change method, and a Bornhuetter-Ferguson method instead of the loss per exposure percent change method.

d. **Reasonableness of conclusions.** The conclusions of the study are reasonable.

- The outstanding losses by coverage are within a range of reasonable outcomes.

The actuary states the older years have seen an improvement, while more recent years seem to have deteriorated. We agree with this conclusion. There are a few instances where the actuary appears to have tempered increases in recent years. As a practical matter, we agree with this approach. Still, the County should closely monitor loss experience over the short term.

The following areas of potential improvements of the study are:

- Net present value calculations of outstanding loss reserves.

- Concise summary tables in the first few pages of the study would greatly help readers understand the analysis and conclusions.

- Better documentation, especially footnotes, will help readers follow the study's logic flow.

3. Adequacy of Funding

The County funds the liability and workers compensation programs separately. Also, the liability program has funds earmarked as primary (claims up to $1.0 million) and catastrophe (above $1.0 million to the self-insured retention [SIR]).

a. Liability

The table below shows the adequacy of funding for primary liability:

Table VII-1
Adequacy of Funding
Primary Liability
(Millions)
As of 12/31/98

(A)	Projected funds available (approximate and unaudited)	$35.7
(B)	Outstanding losses	35.1
(C)	Adequacy of funding (A) - (B)	$0.6

Note: (A) was provided by the County.
(B) is from the actuary's study.

The County has equity of $0.6 million. It is reasonably funded. That is, it has sufficient funds available to meet the outstanding losses ($35.1 million, estimated by the actuary) plus a small amount ($0.6 million, equity) as a buffer against adverse loss experience. We understand the County has historically used the equity as a way to stabilize year-to-year funding.

Based on our discussions with the County, we understand some pending liability claims have taken a turn for the worse. Therefore, a funding shortfall is possible for December 31, 1999.

- The recent deterioration in County liability loss experience threatens the small ($600,000) equity balance in the primary liability fund.

Table VII-1 does not include claims above $1.0 million. Until July 1, 1993, the County did not purchase excess insurance and was financially responsible for all claims. From July 1, 1993 to August 31,1998, the County was insured for claims above $5.0 million. Effective September 1, 1998, the retention was lowered to $2.5 million.

Table VII-2 below shows the adequacy of funding for catastrophe liability.

Table VII-2
Adequacy of Funding
Catastrophe Liability
(Millions)
As of 12/31/98

(A)	Projected funds available (approximate and unaudited)	$17.8
(B)	Outstanding losses	15.8
(C)	Adequacy of funding (A) - (B)	$2.0

Note: (A) was provided by the County.
(B) is from the actuary's study.

The County maintains a separate Catastrophe Fund for liability claims above $1.0 million. The Catastrophe Fund had approximately $17.8 million on December 31, 1998. Through that date, the County's paid loss experience had been excellent, with no claim payments. The actuary has estimated outstanding losses above $1.0 million to be $15.8 million.

Based on our discussions with the County, we understand there have been some incidents that have potential costs well above the $17.8 million in the Catastrophe Fund. It is not possible to determine the ultimate costs. But, should the County have to pay these claims, the $17.8 million will be depleted and additional funding may be needed.

- Incidents with potentially catastrophic results could well exceed the current $2 million surplus in the Catastrophe Fund.

We note that the outstanding losses in Table VII-1 and Table VII-2 include allocated loss adjustment expenses (ALAE). Unallocated loss adjustment expenses (ULAE) are not included.

ALAE are typically legal expenses. For the County, these are external legal expenses (per the study). The County also has significant internal legal expenses (over $2.0 million per year). The internal legal expenses, ongoing administrative and claims management costs are usually classified as ULAE. Such costs will be incurred in the future to settle the pending liability claims.

Recognizing outstanding ULAE in financial statements is required under GASB Statement No. 10. It appears the County has not done so.

- We recommend that the County ask the actuary to include an amount for outstanding ULAE.

b. Workers Compensation

Table VII-3 below shows the adequacy of funding for workers compensation:

Table VII-3
Adequacy of Funding
Primary Workers Compensation
(Millions)
As of 12/31/98

(A)	Projected funds available (approximate and unaudited)	$10.9
(B)	Outstanding losses	20.0
(C)	Adequacy of funding (A) - (B)	($9.1)

Note: (A) was provided by the County.
(B) is from the actuary's study.

- We project the County has a shortfall of $9.1 million (around $7 million, after allowing for investment income). The shortfall is significant, but does not threaten solvency as long as future funding is reasonable.

The amount shown in Table VII-2, Row B, are the outstanding losses estimated by the actuary. We understand the County uses a different amount in its financial statements. It relies on an analysis that does not utilize actuarial procedures and is performed by in-house staff.

We note the in-house staff estimates outstanding losses at $11.9 million as compared to the actuary's $20.0 million estimate. Some of the difference, at most $2.0 million, may be due to anticipated investment income earned on funds held to pay claims. We have been informed that the in-house staff amount reflects anticipated investment income. The actuary's number does not.

We have concerns about using the in-house staff estimated outstanding losses ($11.9 million) as compared to using the amount from the actuary ($20.0 million). This method does not incorporate actuarial techniques (as required by GASB Statement No. 10), is inconsistent with the liability funding approach and raises the question of why the County hires an actuary to estimate its workers compensation losses and then does not use the results.

- We recommend that the County use an actuarial estimate of outstanding losses, discounted for investment income, for financial statement and funding purposes for both the liability and workers compensation programs.

4. <u>Funding Options</u>

We are not aware of any statutory requirements for the County, but most public entities have the option below for funding their self-insured losses. We present them in the order of least to most amount of funds needed.

Primary Liability/Workers Compensation

- Revolving Fund — Money is set aside each year to cover expected claim payments to be made during the upcoming year.

- Revolving Fund Plus Reserve — Money is set aside each year to cover expected claim payments to be made during the upcoming year, plus a reserve is maintained to absorb unexpected payments.

- Actuarial Target — Money is set aside in an amount equivalent to an actuarial estimate of all future loss payments resulting from incidents occurring in the upcoming year, as well as past years.

- Actuarial Target Plus Contingency — Money is set aside in an amount equivalent to the Actuarial Target, plus a contingency is maintained for unexpected losses.

Catastrophic Liability

- Build Contingency Fund — Money is deposited annually until the contingency fund reaches a level that is deemed sufficient to pay for any and all catastrophic losses.

- Other County Funding Sources — No money is set aside to pay for catastrophic losses. If a need arises, other county funding sources are tapped to pay for a catastrophic loss.

The following table compares the advantages and disadvantages of all funding methods:

Table VII-4
County Funding Options

Option (1)	Advantage (2)	Disadvantage (3)
Primary Liability		
Revolving fund	Least amount of funds earmarked of all methods - in theory, only cash needed to make disbursements.	Not actuarially funded. Insufficient revenues to meet expenses - could require County to access additional funds from other sources. Does not match loss cost burden to fiscal period generating the loss.
Revolving Fund Plus Reserve	Target expected claim payments plus unusual payments without upsetting budgets.	Not actuarially funded. Insufficient revenues to meet expenses - could require County to access additional funds from other sources. Does not match loss cost burden to fiscal period generating the loss.

Option (1)	Advantage (2)	Disadvantage (3)
Actuarial Target	Does not require money from the General Fund. Enhances the County's bond rating. Good match of loss cost burden to fiscal period generating loss.	Less money for other County operations. Insufficient revenues to meet expenses if loss experience is worse than expected - could require County to access additional funds from other sources.
Actuarial Target Plus Contingency	Minimizes the potential of needing other resources. Enhances the County's bond rating. Good match of loss cost burden to fiscal period generating loss. Stability of annual contributions even with adverse loss experience.	Least amount of money available for other County operations. County may be tempted to access fund for other operations.
Catastrophe Liability		
Build Contingency Fund	Funds are already earmarked to be used for catastrophic losses when they occur. Provides County with a comfort level.	Large amounts of money set aside and not available for other County operations. Strong possibility in any given year money won't be needed - others may be tempted to access fund for other operations.
Other County Funding Sources	No funds are earmarked to pay for catastrophic losses.	Requires County to access funds, perhaps late in the budget year or at other inopportune times. Could negatively impact County bond rating.

In our experience, we have seen all of the above methods used. The funding approaches used most often are the Revolving Fund Plus Reserve or the Actuarial Target. The Revolving Fund and the Actuarial Target Plus Contingency are rarely used. The County currently uses the Revolving Fund Plus Reserve for workers compensation and the Actuarial Target for primary liability.

The County is exposed to potentially catastrophic losses in a number of areas. Without the Catastrophe Fund, it would have to come up with large amounts of money from other sources to pay for such claims when they occur. Up until now, the Catastrophe Fund has worked as intended in meeting the financial consequences of claims in excess of $1 million. However, more funds need to be accrued to pay for potential losses from recent incidents.

- We recommend that the County obtain an updated actuarial estimate of funds needed for catastrophic losses and accrue the money necessary to meet future obligations.

The best funding method for the County is the one which best matches the County's overall financial strategy. If the County decides not to earmark assets for known liabilities, it will immediately have in excess of $50 million to spend on other operations. However, the County will need to use a substantial amount of revenue to pay for ongoing loss expenses and this approach could negatively impact the County's bond rating.

5. Risk Retention

Generally, the larger the organization, the greater is its risk retention capacity. To determine the dollar amount of accidental losses that an organization can absorb, it must evaluate several subjective and objective factors, including:

a. Unencumbered retained income, reserves or fund balances.

b. Certainty and amount of its annual gross income.

c. Amount of operating and capital expenditures that could be canceled or deferred to meet short-term cash needs occasioned by an accidental loss.

d. Organization's legal and financial ability to issue debt.

e. Ability to increase taxes or otherwise raise revenue to finance accidental loss.

f. Existence of financial reserves designated for catastrophic loss payment.

g. Attitude of senior management toward risk. How willing are elected and appointed officials to face critics following a multi-million dollar loss that may have been insured for a few hundred thousand dollars annually? This is especially true for King County in light of its recent catastrophic losses and legal setbacks.

The County's 1999 economic outlook is for a slowdown. Major factors affecting the County's future are reductions in employment at Boeing (between 7,000 to 10,000 jobs will be lost locally) and weaknesses in Asian markets.

Even with the changes noted in the preceding paragraph, the County has maintained a sound financial base. Nonetheless, with the uncertainty regarding the economy and the fact that the County has experienced some catastrophic losses recently, it must be sure that its risk financing program is appropriate.

Traditional guidelines that relate to an organization's financial data are often used to aid in determining risk retention capacity.

Two of these guidelines are:

a. **Percentage of expenditures.** This method suggests that an appropriate risk retention capacity is indicated by an organization's expenditures. Underlying this guideline is the belief that if an organization suddenly has to finance a large unexpected loss, it will be able to temporarily pare back expenditures previously designated for other uses in an amount sufficient to pay the large loss. A reasonable range often used to establish the amount of expenditures that could be redirected is between 0.5% and 2.0%.

b. **Percentage of unrestricted funds.** A retention amount may be selected based on the amount of an organization's surplus, not designated for another use. This guideline suggests that between 20% and 33% of the unrestricted surplus might be appropriate to use for financing a sudden, large unexpected loss.

Applying the first guideline to the County's data reflects a risk retention capacity of between $8.5 million and $35.0 million (based on $1.7 billion of operating expenditures for 1999 for the agencies covered by the County's self-insured liability and workers compensation programs).

As of December 31, 1998, the County's General Fund held about $26.6 million in undesignated fund balances. Applying the second guideline to the $26.6 million unreserved, undesignated fund balance yields a risk retention capacity of between $5.0 million and $9.0 million.

Based upon the above analysis, our experience with other counties and our discussions with the County's senior financial managers, we judge the County can absorb in a single year up to \$9.0 million of unexpected losses and still meet major operating objectives. The \$9.0 million is in addition to the amount the County has budgeted for expected self-insured losses. For 1999, those amounts are \$6.5 million for general liability, \$6.5 million for automobile liability and \$11.0 million for workers compensation.

Accordingly, the County has a \$33.0 million annual loss retention capacity. This conclusion is a starting point for constructing a risk financing program. It would not be prudent to expose the entire amount to a single loss. Entities ordinarily limit their per loss exposure to no more than 20% of the annual amount. On this basis, the County could retain losses up to \$6.5 million per occurrence (all retentions combined). The current total retention for liability, property and workers compensation is \$3.1 million.

The final retention selected in any single year's program is affected by the relative cost of insurance (or other catastrophic funding options). When insurance pricing is soft, as it is now, the County is able to construct programs that retain less risk than is suggested by the above analysis. Other factors to consider include the economic outlook for the County, adequacy of insurance funds and recent loss experience. Based on all these factors, the County's current retention levels are appropriate.

B. INSURANCE

The County uses insurance to protect against large claims above its retention levels.

1. Liability Risks

In 1961, the Washington State Supreme Court abrogated government immunity for the state. The Legislature followed suit in 1964 for all other local forms of government. Maximum statutory liability limits (tort caps), that protect local government in many states, do not exist in Washington. Attempts were made to institute them in 1981 and 1986, but the State Supreme Court declared them unconstitutional. The Tort Reform Act of 1986 does limit joint and several liability, but it also allows an exception for fault-free plaintiffs.

The County faces a wide variety of tort exposures stemming from its operations. Practically all departments have risks inherent in the services that are provided. These include, but are not limited to, transit, roads, parks, law enforcement, solid waste disposal, wastewater treatment, water and land management, community services, public health, jails, youth services, the airport and development & environmental services. The County also has exposure from its swimming pool and van pool operations. Employment practices, not acceptable in today's business culture, are another key liability exposure for a large employer like the County.

The County provides self-insurance under a formal insuring document for loss up to $2.5 million. A second commercially insured layer provides another $12.5 million of liability coverage to the County above this self-insured layer. The excess $12.5 million layer follows the terms and conditions set forth in the County's written self-insurance program document.

The liability program document now used by the County is modeled after a governmental liability insurance policy often used on the West Coast. It is a broad form that consolidates coverages for many liability exposures (e.g., general liability, law enforcement liability and public officials liability) in one place.

The County's program document is good, but could be even further enhanced. As now structured, finding coverage for a liability claim requires classifying the claim in one of five liability coverages:

a. Bodily injury.

b. Property damage.

c. Public officials.

d. Personal injury.

e. Advertising injury.

Slotting claims into one of these categories is something insurers do more out of custom, than current-day need. Furthermore, the advertising injury category has almost no application in the public sector. The distinction between personal injury and bodily injury is unimportant.

- We recommend the County streamline its program document by amending the insuring agreement to cover all liability for damages caused by an occurrence.

Under this approach, the County would still exclude areas it does not want to cover under the program. However, it would not have to fit each claim into a category. This will simplify coverage determination under the self-insurance program.

The reinsurer should follow the County's approach on this matter, given their high attachment point. Thus, there is less room for a coverage dispute under the simplified model we propose.

Other concerns we have as a result of our review of the self-insurance program document are:

a. **Insuring Agreement.** The insuring agreement states that a continuing loss or a loss arising from a repeated exposure shall be considered one occurrence. However, there is no mention of when the occurrence is to have occurred. To avoid coverage argument and possible denial of a continuous loss in the excess liability, we recommend establishing that a continuous loss or a loss arising from repeated exposures to the same general conditions is considered to occur at the date the damage or injury from the loss was first identified.

b. **Exclusion (F).** Exclusion (F) excludes eminent domain, condemnation and inverse condemnation. However, in some instances property damage claims can be connected with inverse condemnation allegations. For example, if the County altered a levee and a flood later occurred, any allegation that the County's actions on the levee constituted inverse condemnation could cause denial of property damage to nearby resident's property. Instead, despite allegations of inverse condemnation, this exclusion should not apply to the extent there was actual physical destruction to property or loss of use to tangible property.

c. **Exclusion (M), (3).** Exclusion (M), (3) excludes any public officials liability claim which seeks benefits payable under an employee benefit plan and denied because of unlawful discrimination. Most public official errors & omissions coverage forms do not have a similar exclusion. Any denial or reduction of benefits under an employee health plan or pension plan that affects an employee who's race, religion, gender, marital status or disability is identified under civil rights statutes, could be a basis for an uncovered claim.

   For example, if a health provider chosen by the County had a history of limiting treatment on sickle cell anemia, this exclusion could exclude a claim by an employee alleging the County knowingly chose a health provider which regularly denied treatment based on race. Another example is if the County charges more for, or denies coverage under a disability benefit plan due to actual or believed disability, the action could be considered unlawful discrimination under civil rights statutes.

d. **Exclusion (M), (6), (ii).** Exclusion (M), (6), (ii) excludes liability arising out of willful violation of a penal statute or ordinance which is committed with the knowledge or consent of the Named Insured, except that facts known by one insured shall not be imputed to another insured.

The County is identified as the "Named Insured" on the declarations page. The County is a governmental entity represented by its elected and appointed officials, officers and employees. As such, knowledge or consent given by any representative of the "Named Insured" can be argued to constitute knowledge or consent by the "Named Insured." Based on that interpretation, any claim against the County which originates due to deliberate acts by a County representative could exclude the vicarious liability of the County.

We recommend changing the exclusion to say it excludes liability arising out of willful violation of a penal statute or ordinance which is committed with the knowledge or consent of an insured, except that facts known by one insured shall not be imputed to another insured. In that way knowledge by one individual insured who is a representative of the County cannot be imputed to any other individual insured or to the County.

e. **Personal Injury Definition.** The personal injury definition excludes discrimination committed by, or at the direction of the Named Insured. As discussed in item 4, any discrimination deliberately done by a representative of the County could be interpreted to be discrimination by the Named Insured (the County). The County should be covered for vicarious liability arising from the acts of its representatives.

The largest liability claim paid by the County is $2.5 million in 1998, which resulted from a vehicle collision with a guardrail in 1994. Several losses with even larger potential for the County are now pending.

To estimate liability loss potential, we look at potential scenarios with possible severe outcomes. The Kingdome has been the County's largest potential for catastrophic loss because of the crowd exposure. Since it will no longer be owned by the County, we judge the next areas of greatest people concentration to be the courthouse and the detention center. If an incident occurred that caused 1,000 people to each incur, say, $100,000 in damages, resulting liability costs would be $100 million.

Another possible catastrophic exposure would be a loss that arises from a class action suit. A governmental entity could incur multi-million dollar losses in this area. We can see a $20 to $50 million loss potential in this area governed by federal law.

a. **Current risk financing approach.** The County self-insures its liability exposures up to $2.5 million per occurrence. Reinsurers Swiss Re and Employers Re equally share coverage limits of $12.5 million excess of the $2.5 million self-insured retention. Additional liability insurance is purchased in the amount of $87.5 million, bringing total catastrophic loss protection to $100 million in excess of the self-insured retention.

b. **Findings.** Due to the lack of government immunity and tort cap protection and its recent catastrophic loss experience, it is a prudent decision for the County to purchase the amount of excess insurance protection that it has. There can be no guarantee that a loss exceeding the above limits of protection will not occur. Nonetheless, we judge the County's limits to be reasonable.

The County owns an airport that is used mostly by private and chartered jets, including those used by the local professional teams. Occasionally, commercial planes will land at the County's airport when the local commercial airport is too fogged in.

a. **Current risk financing approach.** The County purchases a $300 million policy with a $50,000 deductible for its airport liability exposure.

b. **Findings.** The County's limit of liability purchased is the same amount as that purchased by the local commercial airport. We judge the County's purchase of this policy and the limits to be reasonable.

The County owns six police helicopters that are used for pursuits and rescue operations. The County has not had any claims in this area, but is well aware of the catastrophic potential.

a. **Current risk financing approach.** The County purchases aviation liability insurance with limits of protection in the amount of $50 million.

b. **Findings.** The amount of coverage purchased is sufficient to cover most of the potential catastrophes and is a reasonable amount when considering the cost.

The County has a Van-pool program and purchases liability coverage excess of a $1 million self-insured retention up to the County's overall retention level of $2.5 million. The County purchases protection at the lower limit so that the program would not be technically bankrupted if it incurred a loss in excess of $1 million. In this type of situation, we find that the purchase of such a policy is a reasonable departure from standard practices.

The County purchases a nurses malpractice professional liability policy that covers the County, Seattle King County Department of Public Health, Seattle Public Schools and individual providers specified in the policy. The limit is $5 million each claim and in the aggregate with a deductible of $2,500. The premium of $15,000 is paid by the County and reimbursed by the Health Department.

In May of 1998, Seattle was faced with a reduction in school health services due to cutbacks in school district budgets. To mitigate this crisis, an agreement was reached among Seattle Public Schools, the City of Seattle and the County's Department of Public Health. The plan called for two pilot healthcare delivery models over a two-year period. One model uses school district employed nurses. The other uses personnel hired by clinics and other community healthcare providers.

The school districts and community providers did not wish to assume liability. They requested to be additional insureds on the County's liability program. The County does not provide additional insured coverage for outsiders. To resolve the insurance issue that had deadlocked the contract negotiations, the County decided to buy insurance that would protect all entities involved. This is a good example of how and why risk management decisions should be made in light of all business aspects of an entity's operations.

From a purely risk management perspective, we would not recommend the choice that the County made. However, we find it reasonable that other business considerations would influence the outcome as described.

The County has some pollution coverage in its program document, but has not purchased a separate policy for this specific exposure. Until now, this type of coverage has been limited and very costly. However, there have been signs that broader coverage may be available at more affordable prices.

- We recommend that the County continue to annually review the availability and pricing of pollution coverage to determine if and when it might be a viable product to purchase.

The County also purchases a general liability policy to cover the County's exposure from school district use of the County's pools. Policy limits are $4 million excess of a $1 million SIR. The premium is passed back to the schools through rental fees. The decision to purchase this coverage was based on the fact that the schools refused to reimburse the County for self-insurance. Normally, the County's decision to purchase this coverage is inconsistent and we usually don't recommend it. However, under the circumstances and the adverse situation, we find it to be a reasonable approach.

2. Workers Compensation Risks

The largest probable workers compensation loss would likely arise from an earthquake, fire or explosion at a major administrative center, such as the County Courthouse. One can envision a catastrophe could injure 100 or more employees, each needing substantial medical and wage-loss benefits.

The largest workers compensation claim incurred by the County occurred in 1995. A police officer involved in a high-speed chase was seriously injured in a collision. Estimates of the ultimate loss amount range from $2 - $3 million. Another large loss was incurred by the County in 1997 when one of its utility inspectors was hit by a backhoe. At this point, it is estimated that the ultimate loss will be $600,000.

a. **Current risk financing approach.** The County purchases statutory (unlimited) workers compensation coverage from above a self-insured retention of $500,000.

b. **Findings.** With unlimited insurance limits, we feel that the County has adequate protection for its workers compensation exposure. Since the annual premium is about $70,000, we feel that the purchase of excess coverage is worthwhile considering the County's recent loss experience.

3. Property Risks

The County owns a large amount of property subject to loss or damage from fire, windstorm, explosion, earthquake and other perils. The largest single exposure is the West Point Treatment Plant, valued at about $650 million. Next are the DSTP (tunnel) at $367 million and the Renton Treatment Plant at $333 million. The value of the County's bus fleet is estimated at $264 million, the courthouse at $120 million and the regional justice center at $111 million.

The largest loss in County history occurred in July 1994 when four ceiling tiles fell from the Kingdome. The remaining tiles were removed and replaced. The total cost was in excess of $50 million. Once a new stadium is built next year, the Kingdome will be torn down and the County will no longer have this exposure.

Other than the Kingdome loss, the largest property loss during the last ten years has been around $435,000 in 1991 at the West Point Treatment Plant sewage tunnel. There was also a $342,000 loss in 1992 at the Lake Washington pipeline and a $316,000 loss in 1990 at the North Operations Base parking garage.

a. **Current risk financing approach.** The County has purchased an all-risk property policy with blanket coverage that includes combined property damage and business interruption, boiler & machinery, earthquake, flood and extra expense as its major provisions. Policy limits are $2.5 billion, subject to a $100,000 deductible. The earthquake and flood perils each have a lower limit of $200 million. The earthquake deductible is 2% of the value of the damaged structure, but no less than $250,000. The extra expense limit is $5 million, except $10 million for the courthouse, new jail, general administration building and the West Point and Renton Treatment Plants.

The earthquake coverage was increased last year from $150 million to $200 million. By comparison, the County has some facilities like the West Point Treatment Plant ($650 million), the DSTP ($367 million), and the Renton Treatment Plant ($333 million) which alone are excess of the earthquake limit. Other County buildings are worth in excess of $600 million combined. However, in addition to their insurance coverage, the County would have access to financial relief from FEMA, which was established by the Federal Disaster Relief Act of 1974 (Public Law 93-288). This source of recovery is only available when a community is declared a disaster area following a catastrophic event and when funds are available. Further, recovery is limited to 75% of the loss.

b. **Findings.** The County has some extremely large property exposures and has purchased ample coverage to protect their interests. Despite its limitations, FEMA provides important supplemental protection if the County suffers an earthquake, flood or other similar disaster-type losses in excess of its policy limit.

Willis is obtaining information on Y2K activities of the County to give to insurers. So far, there are no policy limitations regarding this coverage.

4. Alternatives

The County became fully self-insured for liability on April 1, 1986. At that time, only a limited amount of coverage was available and at a high price. A number of public entities chose to form "pools" which, in essence, became the participants' own insurance company. Because of the County's size, pool participation was not a viable option. The County's most likely pooling partners were primarily smaller governments in Washington. The politics of consolidating widely disparate sized entities in a single pool are a challenge few have succeeded in solving.

More recently, however, two pools have been formed to serve large entities like the County. The pools and relevant information are:

a. **National Public Entity Excess Program (NAPEX).** This joint insurance purchasing pool provides liability protection via a broad municipal public entity form on an occurrence basis including coverage for general, public officials errors & omissions, automobile and employment practices liability. Up to $20 million in limits are available subject to a minimum retention of $100,000 per occurrence. Reliance is the lead insurer. Reinsurance support is provided by Munich American Reinsurance. Current local members include the Washington Cities Insurance Authority (WCIA), the Washington Governmental Entity Pool (WGEP), and the Washington State Transit Insurance Pool (WSTIP).

b. **County Reinsurance Limited (CRIL).** It provides liability, workers compensation and property coverage. The pool is actually a mutual insurance company, domiciled in Vermont and formed to serve large counties and county pools. Discover Re reinsures liability excess of $1 million up to $10 million in limits. CRIL provides the difference in limits between the member's SIR and $1 million.

Because such programs can offer catastrophic protection, sometimes at deep discounts, to participants, they are viable to entities like the County.

- We recommend the County evaluate potential participation in these and any similar programs and obtain formal proposals where warranted.

APPENDIX A

KING COUNTY
Executive Response